



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.
- (d) apply to the court for the decision to be reversed or varied. 1 mark**

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.
- (e) Superannuation funds. 1 mark

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 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. 0 marks
- (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. Correct answer
- (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.

9/10 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.

ANS. There are three types of voidable transaction provisions (known as Clawback or anti-avoidance provisions in some other jurisdictions) in the Bankruptcy Act which allow the bankruptcy trustee to bring court proceedings to reverse the effect of: -

- a. Undervalued transactions;
- b. Transfers to defeat creditors; or
- c. Preferential payments to creditors. 1 mark

Most voidable transaction provisions (in both bankruptcy and corporate insolvency) target transactions which occurred during a certain period of time (called the "relation-back period") prior to the "commencement of bankruptcy".

Importantly, the commencement of bankruptcy is not the same as the actual date a debtor becomes bankrupt. In case of involuntary bankruptcy, the commencement of bankruptcy is the time of the commission of the earliest act of bankruptcy occurring within the six-month period immediately before the presentation of a creditor's petition. In the case of voluntary bankruptcy, the commencement of bankruptcy is usually the date that the debtor's petition is presented, but it can be earlier.

Circumstances under which such transactions cannot be reversed

Section 123 - Transactions that 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. 1 mark

Sec-120(6) & Sec-121(8) - 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. 1 mark

0/3 marks - this answer is copied directly out of the Guidance Text

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?

ANS. There are two circumstances under which Article 20 of the Model Law would apply if the stay or suspension arose under:

- (a) the Bankruptcy Act; or
- (b) Chapter 5 (other than Parts 5.2 and 5.4 A) of the Corporation Act, as the case requires.

Accordingly, when an Australian court is considering a recognition application in relation to a corporate debtor, it needs to consider what "the case requires", that is, whether the case requires the broader voluntary administration stay which affects secured creditors or the standard liquidation stay that affects only unsecured creditors. It is not a question of discretion but rather which stay should apply according to the nature of the proceeding. Where the foreign proceeding is clearly a business for foreign proceedings that are more analogous to liquidations. However, difficult questions will be raised where the foreign proceeding is not clearly either business rescue or liquidation like.

0/3 marks - this answer is copied directly out of the Guidance Text

Question 2.3 [maximum 4 marks]

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

ANS. In General, '*ipso-facto* clauses' are clauses which provide contracting parties with a right to terminate a contract in cases where another party is at risk of becoming insolvent.

Role of 'ipso facto' clause under Liquidation Process

The Executory Contracts entered into by a debtor prior to their bankruptcy remains in force even after the debtor becomes bankrupt. The bankruptcy trustee has the benefit of a statutory '*ipso facto*' prohibition, which renders void any provision in a contract that purports to provide a counter-party with a right to terminate, modify or repossess property upon the debtor's bankruptcy.

The bankruptcy trustee is entitled to deny a contract (as well as certain other property such as land burdened with onerous covenants and property that is not readily saleable) by giving written notice to the counter-party, subject to first obtaining the leave of the court if the contract is not an "unprofitable contract". If a contract is disclaimed, the counter-party will have a claim for damages but will be required to submit a proof of debt to recover the loss.

Conclusion

During liquidation process, if a liquidator wishes to maintain an important supply contract for a period of time to facilitate the temporary conduct of the company's business pending as possible sale, the liquidator will not, subject to one exception, have the benefit of the '*ipso facto*' enforcement prohibition that applies during bankruptcy, so that a supplier or other contractor is generally able to terminate its contract with the company as soon as the company enters liquidation (assuming *ipso facto* rights have been incorporated in the contract).

The exception relates to the circumstances where a creditor's voluntary liquidation immediately follows a prior voluntary administration or attempt to negotiate a creditors scheme of arrangement, in which case the *ipso facto* moratorium introduced as part of recent

amendments to the Corporations Act will be invoked. However, while there will be a moratorium in that scenario, the *ipso facto* clause itself will not be void, unlike during bankruptcy.

0/4 marks - the highlighted content in this answer is copied directly out of the Guidance Text

PRELIMINARY TOTAL: 9/20

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.

ANS. Yes, I agree with the above statement that recent reforms have made Australia more of a debtor-friendly jurisdiction.

Situation before the enactment of the New Reforms

1. Australia is considered a creditor-friendly system both generally and in its insolvency process because of the following reasons: -

Unsecured Creditors

2. Unsecured Creditors can bring court proceedings to enforce debts. Smaller Claims will be brought in the Local or Magistrate Courts, where they will be dealt with fairly swiftly and relatively cheaply. Medium size claims will be brought in the Country or District Court. Larger Claims (AUD 1 million and over in most states) must be brought in the Supreme Court of the State or Territory. Claims can be brought in the Federal Circuit or the Federal Court if they also include statutory claims under Federal legislation or if they relate to bankruptcy or corporate insolvency.
3. Unsecured Creditors can issue a specific notice provided for under the Bankruptcy Act and the Corporations Act requiring the individual or company to pay the debt. If the debt is not paid within 21 days after the issue of the notice, the unsecured creditor may apply for the individual to be made bankrupt or for the company to be wound up in insolvency. Failure to comply with this type of demand is an act of bankruptcy by an individual and it creates a presumption of insolvency against an individual or a company. Although the courts have said that this procedure should not be used as a debt collection tool against solvent individuals or companies, it is a highly effective one.

Secured Creditors

4. Secured Creditors are well protected under Australian Law. On World Bank measure, Australia scores an 11 (on a scale of 0-12) for protection of the rights of secured creditors.

Creditors rights in insolvency

5. The primary focus is on the protection of creditor’s rights to the exclusion of management and shareholders, notwithstanding the consequent adverse impact on corporate and business rescue which may be in the interests of employees, small suppliers and other corporate shareholders.

- a. Secured Creditors are entitled to enforce their rights during the bankruptcy process for an insolvent individual and the liquidation process for an insolvent company.
 - b. An alternative aim of voluntary administration is to simply enable a maximum return to be achieved for distribution to creditors.
 - c. Major Creditors with security over the whole or substantially the whole of a company's property remains entitled, subject to compliance with certain time restrictions, to appoint a receiver over the top of a voluntary administrator.
 - d. Non-Major Security creditors, as well as owners and lessors with enforcement rights, can continue with enforcement action which has been commenced prior to the appointment of a volunteer administrator or which relates to a perishable property, or otherwise with the consent of the court.
 - e. Australia has broad insolvent trading liability, which allows a liquidator to recover substantial sums from directors, where the directors have allowed a company to incur debts whilst insolvent.
 - f. Australia's voidable transaction regime, particularly in corporate liquidation, allows transactions to be clawed back for the benefit of creditors over a substantial period of years and without having to prove improper conduct such as an intention to defeat creditors.
6. The Australian Government introduced a "simplified liquidation process" for small companies. It applies to most of the framework of the existing liquidation regime but with adaptations to make the process less complex, less costly, and swifter, so as to ensure greater returns of creditors and employees.

Conclusion

However, the corporate voluntary administration regime and some recent reforms to the corporate insolvency process in Australia are designed to encourage a stronger corporate and business rescue culture and promote a move away from the existing dominance of creditors rights. Specifically: -

- a. the **voluntary administration regime** has its primary goal the maximization of the chance of an insolvent company, or as much as possible of its business, continuing in existence under the terms of a DOCA.
- b. Subject to certain exclusions, as of 1st July, 2018, creditors are prevented from enforcing ipso facto contractual rights contingent only on a company's insolvency or enter into an external administration. The personal insolvency regime takes an even stricter approach, with the Bankruptcy Act rendering ipso facto clauses void outright when a person becomes bankrupt and
- c. as of September 2017, company directors can take advantage of a "**safe harbour**" from insolvent trading liability, so that they can continue to allow a company to incur debts with a view to implementing an informal restructuring attempt under the supervision of an appointed expert restructuring expert.

0/15 marks – the highlighted content in this answer is copied directly out of the Guidance Text

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 Lyonessean. 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 Lyonessean 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 Lyonessean 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 Lyonessean liquidation.

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

ANS. The ATO should immediately move an application before the Federal Court for modifying the recognition orders as a 'foreign main proceeding' and giving leave to ATO to take steps for enforcing its claim in Australia, expressly for the purpose of recovering an amount up to the *pari passu* amount the ATO would have received if they were entitled to prove for the tax debt as an unsecured creditor in the foreign main proceeding.

The ATO can reply on the Judgment upheld in the matter of 'Ackers v. Deputy Commissioner of Taxation' (2014) 223 FCR 8; [2014] FCAFC 57, which was similar to the facts of the present dispute. **Correct.**

You did not spot the other issue: there is a real question on the facts about whether HA's COMI is in Lyonesse, or in Australia.

3/9 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?

ANS. The HA should opt for **Voluntary administration**. **Yes, but why?**

A company can enter Voluntary administration after a majority of the company's directors resolve that in their opinion the company is insolvent or is likely to become insolvent at some future time and that an administrator should be appointed. Actual insolvency is not required and likelihood of insolvency at some future point time is sufficient]

Before the introduction of the safe harbour in section 588 GA of the Corporations Act, directors of a company would typically appoint a voluntary administrator at the first sign of financial trouble in an attempt to avoid personal liability for insolvent trading (by invoking the defence to liability under Section 588 H (6) of the Corporations Act. While Voluntary administration is a formal corporate rescue mechanism in Australia, in practice the previous experience was that the appointment of a voluntary administrator would invariably cause creditors to invoke their ipso facto contractual rights and/ or enforce their securities where the voluntary administration moratorium did not apply. That outcome compromised the success of a formal corporate or business rescue attempt under a DOCA.

1/6 marks – all but one sentence of your answer was copied directly from the Guidance Text

*** End of Assessment ***

TOTAL MARKS: 13/50