



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. **Correct answer**
- (d) A deed of company arrangement. **0 marks**

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. **0 marks**
- (d) The bankrupt’s family home.
- (e) Superannuation funds. **Correct answer**

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 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.

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.

Per the Bankruptcy Act the bankruptcy trustee may bring court proceedings to reverse the effect of:

- undervalued transactions
- preferential payments to creditors
- transfers to default creditors

In respect of undervalued transactions if the transferee were able to show that the transaction occurred more than two years prior (or four years for related party transactions) and could demonstrate that the debtor was solvent at the time of the transfer it is likely the bankruptcy trustee's proceedings would not be successful.

In relation to preferential payments, were a creditor able to show that it received the payment from the company in good faith, in return for valuable consideration and in the ordinary course of business then the transaction would not be reversible.

With regards to transfers to default creditors, were the transferee able to demonstrate that it paid market value for the property and that at the time of the transfer they did not know or could not have reasonably deduced that the transferor's main purpose was to defeat creditors or that the transferor was insolvent or about to become insolvent then the transaction would not be reversible.

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?

Australia has defined the scope of the stay under Article 20 of the Model Law as being the same as would apply if the stay arose under:

- The Bankruptcy Act; or
- Chapter 5 (other than parts 5.2 and 5.4A) of the corporation's act, as the case requires.

In the case of a corporate debtor the Australian Court needs to consider what "the case requires" i.e. whether the case requires the broader voluntary administration stay, which affects secured creditors, or, whether the case requires the standard liquidation stay which only affects unsecured creditors. Which stay the Court should apply is not a question of discretion but rather an assessment of the nature of the proceeding in question.

If for example the application being heard was in relation to a foreign proceeding that is a business rescue procedure the broader voluntary administration stay would likely be more appropriate. If however, the application was for a foreign proceeding that was more akin to a liquidation then the standard liquidation stay would likely be more appropriate. Should the foreign proceeding not be clearly either a business rescue or a liquidation then the Court will have a harder task determining the appropriate stay.

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?

An *ipso facto* clause is a provision in an agreement which permits its termination due to the bankruptcy, insolvency or financial condition of a party.

Typically executory contracts entered into by a debtor prior to their bankruptcy remain enforceable once the debtors becomes bankrupt. However, 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, in accordance with section 301 of the Bankruptcy Act. This covers provisions in a contract such as an *ipso facto* clause. **This question is about company liquidations, not personal bankruptcies.**

The *Ipso Facto* moratorium commenced operation on 1 July 2018, following the passing of the Treasury Laws amendment Act 2017.

Liquidations do not get benefit of *ipso facto* protection. However, *ipso facto* clauses that are triggered by a prior voluntary administration or attempt to negotiate a creditors' scheme of arrangement continue to be subject to the moratorium during a subsequent liquidation.

1.5/4 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.

Australia is considered to be very creditor friendly for a number of reasons. Firstly, unsecured creditors of any size can bring court proceedings to enforce debts swiftly, regardless of the size of their debt, particularly in respect of small claims which are typically dealt with swiftly and cheaply by the Magistrates Courts. To bring court proceedings unsecured creditors must issue a specific notice provided for under the Bankruptcy Act and the Corporations Act requiring the company to pay the debt. If the debt is not subsequently paid within 21 days of the notice being issued the unsecured creditor may apply for the company to be wound up in insolvency. Failure to comply with this type of demand creates a presumption of insolvency against the company and whilst the Courts advise against using the process as a debt collection tool against solvent companies it can be exploited as such and is highly effective should a creditor seek repayment of a debt from a solvent company. **Although this is correct, this is not relevant to Australia’s reforms which have made Australia more debtor-friendly.**

Further the primary focus of Australia’s insolvency regime is the protection of creditors’ rights to the exclusion of management and shareholders, regardless of the potential adverse impacts on corporate and business rescue which may be in the best interest of other stakeholders such as employees, small suppliers etc. For example, secured creditors are able to enforce their rights during the liquidation process of an insolvent company. In addition, major creditors with security over the whole or a substantial portion of a company’s assets remain entitled (subject to certain time restrictions) to appoint a receiver over the top of a voluntary administrator. This despite one of the stated aims of voluntary administration being to maximise the chance of an insolvent company (or as much as possible of the business) continuing in existence under the terms of a DOCA. **Again – this does not directly address the question.**

Also in creditors favour is the broad insolvent trading liability provision which allows a liquidator to recover substantial amounts from directors where the directors have allowed a company to incur debts whilst insolvent. Such recoveries typically are paid from a directors’ or officers’ insurance policy, D&O policy.

In addition, Australia’s voidable transaction regime provides for the benefit of creditors, the ability for transactions to be clawed back over a substantial period of years and without having to prove improper conduct such as an intention to defeat creditors.

Finally, per the Australian insolvency regime, non-major secured creditors (as well as owners and lessors with enforcement rights) have the ability to continue with enforcement action provided that:

- It was commenced prior to the appointment of a voluntary administrator; or
- Related to perishable property; or
- Otherwise with the court’s consent.

Whilst the above does demonstrate the creditor friendly characteristics of Australia’s insolvency regime recent reforms to the corporate insolvency process **the regimes you have summarised above are not recent reforms to the corporate insolvency process** and the introduction of the corporate voluntary administration regime demonstrate that there is a drive to encourage a stronger corporate and business rescue culture in Australia, signally a move away from the current dominance of creditors’ rights.

Relevant to this include changes such as the safe harbour for directors from insolvent trading liability, effective as of 19 September 2017 (introduced by the Treasury laws amendment act 2017). This enables company directors to continue to allow a company to incur debts with a goal of implementing an informal restructuring attempt (under the supervision of an appointed restructuring expert). **Yes**

In addition, as of 1 July 2018 creditors are prevented from enforcing ipso facto contractual rights contingent only on a company's insolvency or entry into an external administration. However, there are exceptions to the ipso facto moratorium for example it will not apply where a creditor seeks to enforce a contractual right on the independent basis that a company had not complied with a payment or performance obligation after it enters voluntary administration. **Yes**

In conclusion it is evident that whilst Australia was considered a very creditor friendly jurisdiction it is making strides to improve the balance between creditors and other stakeholders interests through various reforms. However, as detailed above the reforms themselves have exceptions and therefore may not be practicable in certain circumstance. Further, whilst there is reform in the regime it will take time for this to flow through to the actions of creditors in insolvency proceedings and will require a culture shift at a corporate level to make the reforms truly effective.

8/15 marks – you mentioned a few developments in the insolvency space which have sought to improve the rights of debtors. The first half of your essay, however, did not directly answer the question. There are a number of other debtor-friendly initiatives which you could have mentioned. For example, the new small company restructuring regime for small businesses is very debtor-friendly as it is essentially a debtor-in-possession regime (just with the supervision of an IP).

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 Lyonessian liquidation.

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

ATO could look to the decision of the Full Court of the Federal Court of Australia in the case *Ackers v Deputy Commissioner of Taxation*. The facts of the case resemble that of Aussiebee and ATO in that in the *Ackers* case the Cayman Islands liquidation of a Cayman Islands registered company had been recognised as the foreign main proceeding in Australia and the foreign representative wished to remit approximately AUD \$7M from the sale of Australian assets to the Cayman Islands for distribution of the estate. However, the company owed \$83M in taxes in Australia and a debt payable to a foreign revenue creditor is not admissible to proof in a Cayman Islands liquidation (as is the case in ATO's scenario and its claim not being admissible in the Lyonessian liquidation). In *Ackers*, on the application of the deputy commissioner of taxation ("DCT") the Federal Court modified the recognition orders giving the DCT the right to take steps to enforce its claim in Australia, expressly for the purpose of recovering an amount up to the *pari Passu* amount the tax authority would have received were it entitled to prove for the tax debt as an unsecured creditor in the Cayman Islands main proceeding. The Federal Court's decision was upheld on appeal by the Full Court which found that the modification of the recognition order was an appropriate way to ensure that the interests of the tax authority as a creditor were adequately protected.

Should the liquidator appointed to Aussiebee be successful in obtaining recognition in the Australian court of the Lyonessian liquidation as the foreign main proceeding then the ATO could make a similar application as the tax authority in *Ackers* seeking the right enforce its claim of AUD \$13M in Australia. This could take the form of seeking a portion of the proceeds that may arise from the sale of Aussie's shares in NewYums and could result in a significant recovery for the ATO. In addition, it appears that Aussiebee has additional assets in its own name in Australia in the form of offices and warehouses and the ATO could seek to claim a portion of any proceeds from the sale of such assets should it be successful in obtaining an order to enforce its rights in Australia.

The ATO also has its own fund available to it for funding litigation by liquidators where there is likely to be a return to the tax office on its proof of debt if the litigation was successful. This would likely be a secondary approach for the ATO and would only be applicable if they obtained the order to enforce their rights in Australia, there was potential litigation identified by the liquidator and the jurisdiction of the litigation and associated recoveries were in Australia such that the ATO would be able to claim against them for their outstanding debt. Further information outside of that provided in the question would be required to determine if this was a feasible option. **Interesting extra point.**

You missed the second main point. The ATO should intervene on the recognition application, arguing that the COMI of Aussiebee is Australia, not Lyonesse, and so the assets of Aussiebee 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.

5/9 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?

One possible option for the board of HA to consider would be the commencement of a voluntary administration, given that the Perth re-refining plant appears to be a profitable operation and could be continued thus likely protecting jobs. However, this may not be a viable option given that the directors have advised that all possibilities for refinancing HA's debts have been exhausted therefore it is unlikely that a restructuring plan could be formulated. **Can use VA even when hopelessly insolvent without viable options.**

The directors of HA could seek a debtor in possession process such as a scheme of arrangement, whereby the directors would play an active role in negotiating the terms of the scheme with creditors and subsequently remain in office pending the implementation of the scheme (subject to any terms of the scheme to the contrary). This is a court driven process with a minimum of two court hearings before the scheme can become effective.

The directors should also be made aware that should a liquidator be appointed over HA (following the commencement of proceedings by BOR, CBA or the shareholder of HGL should HA not be able to make its loan repayments commencing in 2022) they may have cause to bring action against HA's directors (and HGL as the holding company of HA) for fraudulent insolvent trading given that the directors appear to have been aware the company was insolvent from October 2020 but continued to incur further debts to trade creditors and the loan obtained from HGL. On the background presented it would appear there would be strong grounds for an insolvent trading claim against the directors. The directors would not be able to cite the safe harbour from insolvent trading provisions as protection as they have not met the conditions for such to be applicable such as proceeding and implementing a restructuring plan made in consultation with an expert advisor. **Good point.**

In respect of the security granted to CBA over HA's three trucks, as the associated mortgages have not been registered on the Personal Property Securities Register it is unperfected and therefore the three trucks (being the security interest in question) would automatically vest in HA (being the grantor) immediately prior to the commencement of voluntary administration proceedings or a liquidation of HA. **Well spotted.**

The Board should resolve to place HA into voluntary administration, resolving that it is insolvent or likely to become insolvent. They need to be aware that:

- **The *ipso facto* clause in the loan agreement will not be triggered by entry into VA (but it will trigger once the company then goes into liquidation or a DOCA after the VA period).**
- **As you noted, immediately before HA enters voluntary administration, the mortgages over the trucks will vest in the voluntary administrator.**
- **The VAs, or HGP, could propose a DOCA if HGP is willing to tip in some cash to create a fund to pay creditors (which would incentivise creditors to vote for the DOCA), or if they can find a purchaser for the Perth plant.**
- **All creditors will get to vote on the DOCA, HGP appears to only be owed \$5m so it will not be able to out-vote the other creditors. But HGP's major shareholder is the major creditor of HA, so they will out-vote the other creditors and will presumably want a DOCA rather than a liquidation.**

4/6 marks

*** End of Assessment ***

TOTAL MARKS: 30/50