



**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. 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. 0 marks
- (d) the directors resolve that the company is insolvent or likely to become insolvent. Correct answer

### 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.
- (d) is an agent of the company until the appointment of a liquidator to the company. 1 mark
- (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.

The three voidable transactions that can be reversed are:

- undervalued transactions;
- transactions to defeat creditors; and
- preferential payments to creditors.

These transactions are not reversible if the transaction was undertaken in good faith, in the ordinary course of business and without a petition by a creditor or debtor. Additionally, if the property acquired in the voidable transaction is subsequently transferred by the transferee to a third party, who received the property in good faith and for market value.

3/3 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?

In determining the scope of the stay, the Court has to consider whether to apply the stay as applied under the voluntary administration regime (which applies to secured creditors), or the stay under the liquidation regime (which only applies to unsecured creditors). In making this determination, the Court has to consider what the case requires and whether the foreign proceeding is more like a business rescue procedure, which requires the voluntary administration stay, or more akin to a liquidation and requires the liquidation stay.

2/3 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 contractual right that allows a party to a contract to terminate the contract by virtue of the counterparty being subject to an insolvency process. In a liquidation, creditors are entitled to rely on ipso facto clauses in contracts and terminate the contract, whereas there are prohibitions on enforcing these rights in a voluntary administration. The only situations in which a moratorium on creditors enforcing ipso facto rights is when the liquidation occurs after a voluntary administration or an attempt to negotiate a creditors' scheme of arrangement.

Because *ipso facto* clauses are enforceable in a liquidation, this impacts the Liquidators' ability to continue to trade the business as suppliers may simply terminate the contract, or hold the Liquidator to ransom by requiring payment of outstanding balances before they provide further supply.

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 (although, going beyond what is in the Guidance Text, there is continuing uncertainty about how these provisions operate because most ipso facto clauses will also trigger independently on the commencement of the liquidation).

**3.5/4 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 has traditionally been considered a more creditor friendly system. The key attributes that define this are the rights afforded to creditors in an insolvency scenario, the risks posed to directors from insolvent trading and the lack of debtor in possession insolvency proceedings. Key features of the Australian regime are:

- Secured creditors retain substantial enforcement rights in an insolvency proceeding. This includes the ability to appoint a receiver in a liquidation to realise assets subject to their security;
- While the stated aim of a Voluntary Administration is to rehabilitate the Company, an alternative outcome is to ensure a better return to creditors than from a liquidation. Additionally, in a Voluntary Administration, a secured creditor with a security over the whole or substantially the whole of the company’s property can appoint a receiver over the top of the Administrator, which may potentially frustrate the goal of rehabilitating the company;
- The key insolvency proceedings available for most companies (Voluntary Administration, Receivership and Liquidation) require the appointment of external insolvency practitioner, rather than allowing for a debtor in possession proceeding;
- Directors are subject to significant risks relating to insolvent trading if they continue to trade a company that is facing potential insolvency. This makes it significantly more risky for directors to continue trading a company to restore it to solvency; and
- The Voidable trading regime allows Liquidators to examine transactions over a long period of time and unwind the transactions for the benefit of creditors.

Accordingly, relative to other systems, notably the US and UK systems, the Australia system is more creditor friendly. There have been some recent changes that make Australia more debtor friendly, including:

- As of 1 July 2018, creditors are no longer entitled to enforce ipso facto contractual rights in an Administration. This affords a greater opportunity to try and restructure or rehabilitate the company as the Administrator can continue to trade the company and maintain critical contracts while investigating the ability to enter a DOCA; **Good**
- The institution of a safe harbour regime, that provides directors with protection from insolvent trading while they try and successfully restructure the company under the supervision of a restructuring professional; **Good**
- The creation of a new small business restructuring process, which allows management to remain in control of the company while they develop a restructuring plan with the assistance of a restructuring practitioner. The process provides similar protections to the Voluntary Administration regime, including moratorium rights and protection against ipso facto contractual rights. **Good**

These changes go some way to making Australia more debtor friendly, as they provide greater support for restructuring a company for the purposes of rehabilitating it (as opposed to liquidating it) and allowing for management to develop solutions, rather than having to immediately appoint an insolvency practitioner. However, an impediment to restructuring of businesses being successful is the anti-collectivist culture that remains in Australia.

12/15 marks – you have mentioned the key developments to improve the rights of debtors in Australia’s insolvency system. Your essay could have been strengthened by providing more detail as to the recent changes. Further, you could have mentioned the increase in creditors’ procedural rights in the insolvency process (such as the right to require IPS to provide information or rights to vote out IPs more easily).

#### **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?

In this case, the Lyonessian Liquidators are seeking recognition and an ability to realise Australian based assets for the benefit of Lyonessian creditors. Given the ATO cannot claim in the Aussiebee liquidation, if the funds are remitted to the Lyonessian Liquidators the ATO will not make any recovery in the Aussiebee liquidation. Accordingly, the ATO needs to seek some protection to allow it to claim against the funds.

While Aussiebee is not an Australian registered company, the Corporation Act applies to Aussiebee as it was an unregistered foreign company that was carrying on business in Australia. **Good** The ATO could therefore apply to Court to have a Liquidator appointed to the company on the basis of the insolvency, being evidenced by the appointment of Liquidators in Lyonesse and the non-payment of taxes. If an appointment was made, then the Court would need to consider whether the Lyonesse Liquidation or the Australian Liquidation was the foreign main proceeding. In this instance, while there are some factors indicating Australia (the board is Australian based, its operations are partly based in Australia, and it has Australian offices), the Court may decide the COMI is in Lyonesse due to the registration and the CEO is based in Lyonesse. This would impact the relief available for the Lyonesse Liquidators. **Good**

There is another path for the ATO, following the Court's decision in *Ackers v Deputy Commissioner of Taxation* (2014) 223 FCR 8. In the circumstances, the ATO could apply to Court to seek a modification of the recognition orders so that the ATO can enforce its claim in Australia to enable it to recover an amount on a pari passu basis as if they had claimed in the Aussiebee liquidation. This is the path the ATO took in similar circumstances in *Ackers* and the ATO was successful. Accordingly, this option is recommended for the ATO. **Good**

**9/9 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?

HA is insolvent on the basis that it cannot meet the judgment debt and the CBA debt. The board needs to urgently act to prevent further loss to creditors and to manage the ongoing risk of personal liability from insolvent trading. While the board could seek to avail themselves of the protections under the safe harbour regime while they develop a solution, the board have indicated there is no more funding, the trading is not sufficient to cover the debts, and they have exhausted all possibilities for refinancing the debts, so this would not necessarily be useful. **Correct** In the circumstances, the board will need to consider appointing an insolvency practitioner to manage the company's insolvency. The board is able to appoint Administrators to the company on the basis the company is insolvent. **Yes.**

This will not avoid the risks faced by the directors for trading to date **It could if they can stay out of liquidation.** By continuing to trade beyond October 2020, the directors of HA have put themselves at risk of personal liability for debts incurred between October 2020 and the date of insolvency. This is because the company was insolvent at October 2020, there were reasonable grounds for suspecting the insolvency, and the directors failed to prevent HA incurring the debt. Furthermore, HGL as the parent company may also be liable for some of the debts of HA under section 588v of the Corporations Act 2001.

If the company enters any form of restructuring or insolvency process, the funding for the Perth plant of \$AU30 million will also become due and payable. This is an unsecured debt only and will rank equally with the judgment debt. **It would be subject to a moratorium while the company is in a voluntary administration.**

HGL has provided funding to HA which will now also be an unsecured claim against HA. However, these claims are effectively subordinated to all other unsecured creditors. **Debts to related companies and holdings companies are not subordinated in Australia. Only shareholder claims "arising from a person buying, holding, selling or otherwise dealing in shares in the company" are subordinated.**

The board of HA will need to consider the impact of the insolvency of HA on HGL, with reference to the potential claims against HGL and the subordinated loan to HA. The board should undertake a detailed assessment of the solvency of HGL so as to avoid trading while insolvent. The board may need to consider whether the safe harbour provisions should be involved to provide protection through this period.

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).
- Immediately before HA enters voluntary administration, the mortgages over the trucks will vest in the voluntary administrator because CBA failed to register its security interests on the PPSR. 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 trucks to create a fund to provide a return to unsecured creditors.
- 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.

**2.5/6 marks**

**\* End of Assessment \***

**TOTAL MARKS: 41/50**