INSOL INTERNATIONAL
FOUNDATION CERTIFICATE
IN INTERNATIONAL INSOLVENCY LAW

# SUMMATIVE (FORMAL) ASSESSMENT (RESIT SEPTEMBER 2022): MODULE 8A

# AUSTRALIA

This is the **summative (formal) resit assessment** for **Module 8A** of this course. Please read the instructions on the next page very carefully.

**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.assessment8Aresit]**. An example would be as follows 202223-336.assessment8Aresit. **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. This assessment must be returned to David.Burdette@insol.org by e-mail no later than **23:00 (11 pm) BST (GMT +1) on Monday 26 September 2022**. When returning the assessment by e-mail, your e-mail must confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words**.

6. Prior to being populated with your answers, this assessment consists of **9 pages**.

**ANSWER ALL THE QUESTIONS**

Commented [DB1]: 29 out of 50 = 58%

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

Commented [DB2]: 8 out of 10

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and mark your selection on the answer sheet by highlighting the relevant paragraph **in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

**Question 1.1**

**Select the correct answer:**

If a creditor is dissatisfied with the bankruptcy trustee or liquidator's decision in respect of its proof of debt, the creditor may:

(a) apply to AFSA or ASIC for the decision to be reversed or varied.

(b) apply to the bankruptcy trustee or liquidator for the decision to be reversed or varied.

(c) bring court proceedings for a money judgment in respect of the debt.

(d) apply to the court for the decision to be reversed or varied. Yes

**Question 1.2**

Which of the following **is** a debtor-in-possession process?

(a) Small company restructuring. Yes

(b) Bankruptcy.

(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. Yes

(b) Deed of company arrangement.

(c) Creditors' voluntary liquidation.

(d) Voluntary administration.

(e) Small company restructuring.

**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 100,000 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 debt agreement under Part IX.

(b) A voluntary administration followed by a deed of company arrangement.

(c) A small company restructuring.

(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. Yes

**Question 1.6**

Which of the following claims **are not provable** in a liquidation?

(a) Future debts

(b) Contingent claims

(c) Penalties or fines imposed by a court in respect of an offence against a law

(d) Claims for damages for personal injury

**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. Yes

**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. Yes

(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. Yes

**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. Yes

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

(d) A safe harbour from insolvent trading liability.

**QUESTION 2 (direct questions) [10 marks]**

Commented [DB3]: 7 out of 10

**Question 2.1 [maximum 3 marks]** 2 marks

Name the five types of voidable transactions that can be reversed by a liquidator on application to the court, and explain whether it is a complete defence to each of these types of voidable transactions if the defendant proves that they were not aware that the company was insolvent at the time they entered into the transactions.
[Type your answer here]

**Part A:**

A liquidator has the authority to forgo transactions under Part 5.7B of the Corporations Act if they are:

a. Unfair preferences: transaction

b. Uncommercial transactions
c. Unreasonable director-related transactions
d. Unfair loans
e. Circulating security interests

**Part B:**

It is true that an absolute defence for unfair preferences and ad hoc/uncommercial transactions exists if the defendant can show that they were unaware the business was bankrupt when they entered into the transactions.

However, unlike unfair preference and uncommercial transactions, an unreasonable director-related transaction of the company can still be recovered from, even if the company was not insolvent at the time the transaction was entered into or did not become insolvent as a result of doing so. Thereby making it an incomplete defence for such transactions.

The same is true for unfair loans, which the liquidator may contest regardless of whether the company was already insolvent or became so as a result of the loan.

Additionally, a circulating security interest is only valid if it was created within six (6) months of the start of the liquidation and securing prior debt.

**Question 2.2 [maximum 3 marks] 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]

**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.

**Question 2.3 [maximum 4 marks]** **2 marks**

What are the differences between liquidations and small company liquidations?

[Type your answer here]

Your answer is too long for 4 marks and you have not read the question properly!

**Introduction:**

For enterprises with liabilities under $1 million, a simplified liquidation process is a streamlined creditors' voluntary winding up. It only applies to voluntary winding ups by creditors of companies when the initiating event takes place on or after January 1, 2021.

The following requirements must be met in order for a company to be eligible for the simplified liquidation procedure:

- the company must be in a creditors' voluntary winding up, with the event that initiates the winding up occurring on or after January 1, 2021;
- the liabilities of the company on the day a liquidator is first appointed in the creditors' voluntary winding up must not exceed $1 million;
- the company will not be able to pay its debts in full within twelve (12) months; and the directors must act within five (5) business days
    - a report on the financial situation of the firm
    - a declaration that they believe, on reasonable grounds, the company meets the eligibility criteria for the simplified liquidation process will be met

The following additional conditions must be met:

- the company has not undergone restructuring or been the subject of a simplified liquidation process in the previous seven years;
- no person who is a director of the company, or who has been a director of the company within the past year before the date a liquidator was first appointed, has been a director of another company that has been subject to those processes.

**Simplified liquidation process for creditors' voluntary winding up:**

If the qualifying requirements are completed and not more than 20 business days have passed since the liquidator was originally appointed in the creditors' voluntary winding up, the liquidator may choose to use the streamlined liquidation process. However, before implementing the streamlined liquidation procedure, the liquidator must have given written notice to each member and creditor at least 10 working days in advance of a declaration that they have reason to believe that the simplified liquidation process' eligibility requirements will be met; an explanation of the simplified liquidation process; a declaration that they will not use the simplified liquidation process if at least 25% of the creditors' total value instruct the creditor in writing not to use the simplified liquidation process; and any required information on how the creditor may ask the liquidator not to use the streamlined approach in writing. If more than 25% of the value of the creditors request in writing to the liquidator that the streamlined liquidation procedure not be followed before the liquidator adopts it, the liquidator shall not use the simplified liquidation process.

If the liquidator has reasonable grounds to believe that the company, or one of its directors, has engaged in conduct that involves fraud or dishonesty and that conduct has had, or is likely to have, a materially adverse effect on the interests of creditors as a whole or a class of creditors as a whole, then the liquidator must stop using the simplified liquidation process. Also, if the simplified liquidation process' eligibility requirements are no longer met.

**Liquidation vis a vis Small Company Liquidation:**

- In a streamlined liquidation process, creditors' meetings are not held. Through the "proposal without a meeting method," matters agreed by creditors are resolved without a meeting. Additionally, creditors cannot establish an inspection committee. Okay
- Within three months of their appointment, liquidators in streamlined liquidations are required to provide creditors a report on any work they have completed thus far, their predictions for when the liquidation would be completed, and their chances of receiving a dividend.
- No further reports to creditors are required. In a streamlined liquidation procedure, creditors have the right to ask the liquidator for information in a fair manner.
- The liquidator is only permitted to make a dividend payment to creditors if money will be available to do so. Since the administration is likely coming to an end at this point, there is no way to distribute interim dividends.
- In a streamlined liquidation process, the liquidator must notify ASIC of any alleged misconduct if the liquidator has reasonable grounds to think that conduct that would be illegal under federal, state, or local law with regard to the company may have taken place; or the action has or is likely to have a materially negative impact on the interests of creditors generally or of a class of creditors generally. Okay

The answer was:

The simplified liquidation process applies most of the features of a regular liquidation, except for the following key modifications:

- clawback of voidable transactions will only apply to unfair preferences of over AUD 30,000 that were paid to related parties of the company in the three months prior to the commencement of the liquidation;
- liquidators are only required to report to ASIC on potential misconduct where there are reasonable grounds to believe that misconduct has occurred (which eliminates the significant time and cost otherwise required to investigate all conduct before reporting to ASIC);
- removal of the requirement to hold creditor meetings and the removal of committees of inspection;
- simplification of the proof of debt process and the dividend process;
- provisions for electronic communications and voting.

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

**Commented [DB4]:** 8 out of 15

"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]

**Introduction:**

I disagree with the aforementioned claim that Austalia is becoming more debtor-friendly from being creditor-friendly. Australia's restructuring and insolvency procedures are generally considered 'creditor-friendly' examples?, focused on achieving the best return for creditors. 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 practiced 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; although 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 DOCA as its main objective. Additionally, starting of July 1, 2018, creditors are prohibited from asserting claims based only on a company's insolvency 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 overcome the slowdown of economic activity caused by the COVID-19 outbreak and related emergency measures implemented to tackle the health crisis have led to severe difficulties for companies to meet their financial obligations. Many of the fixed costs, such as rents and interest payments, remain due while the cash flow destined to meet these obligations has

vanished. As a result, many otherwise sound companies are facing acute liquidity constraints that eventually might become solvency problems. Thus, in order to mitigate liquidity shortages and avoid unnecessary bankruptcies that may follow from the COVID-19 pandemic, national authorities adopted the certain temporary measures.

**COVID-19 related Amendments:**

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.

**Rights of Creditors in Australian Insolvency Domain:**

Australia is regarded as a creditor-friendly country because of its emphasis on safeguarding creditors' interests in insolvency situations,. For instance, practically all bankruptcy and insolvency procedures in Australia require the appointment of an administrator rather than procedures where the debtor is in possession (except schemes of arrangement, and small business restructurings although there also a qualified insolvency practitioner will have to be appointed as an advisor). During the insolvency and liquidation proceedings, secured creditors have the right to assert their claims, and major creditors having security over all or nearly all of a company's assets have the right to appoint a receiver instead of a voluntary administrator. Australia has 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.

**Secured Creditors:**

Under Australian law, secured creditors are well-protected. Australia receives an 11 out of 12 points from the World Bank for protecting secured creditors' rights.

The secured creditor under the Australian regime is bestowed with many rights some of them are mentioned herein-below:

- During a company's liquidation and the bankruptcy process for insolvent individuals, secured creditors have the right to assert their claims. The principal official corporate rescue procedure in Australia, voluntary administration, has as one of its stated goals increasing the likelihood that a firm, or as much of its activity as is possible, will continue to exist.

- Subject to meeting specified deadlines, major creditors who hold security over all or nearly all of a company's assets retain the right to name a receiver instead of a voluntary administrator or administrator.

- Owners and lessors with enforcement rights, as well as non-major secured creditors, may continue with enforcement actions that were started prior to the appointment of a voluntary administrator or that pertain to perishable property, or otherwise with the court's permission;

- Australia's voidable transaction legislation permits transactions to be clawed back for the benefit of creditors over a significant number of years, especially in corporate liquidation. When directors permitted a firm to accumulate debts when it was insolvent, liquidators may be able to recover significant amounts from them (often through a directors' and officers' insurance policy).

- The basic objective of the voluntary administration system is to increase the likelihood that an insolvent firm, or as much of its activity as is possible, will continue to operate under the conditions of DOCA. It is intended to support a shift away from the current dominance of creditors' rights and to foster a stronger corporate and business rescue culture.

- As of July 1, 2018, creditors cannot enforce contractual rights that are only triggered by a company's bankruptcy or admission into an external 14 administration. Company directors have access to a "safe harbour" from liability for insolvent trading as of September 2017. In the event of bankruptcy, ipso facto clauses are completely void under the Bankruptcy Act.

**Unsecured Creditors:**

Unsecured creditors can instate the bankruptcy and or insolvency proceeding by issuing a specific notice provided for under the Corporations Act requiring the individual or company to pay the debt. Failure to comply with this type of demand is an act of bankruptcy against an individual and it creates a presumption of insolvency against a company. Furthermore, Unsecured creditors have the right to file legal actions to collect

debts. Smaller claims will be filed at the Local or Magistrates Courts, where they will be handled fairly quickly and inexpensively. Claims of a moderate scale will be filed at the district or country court. Larger claims (AUD $1 million and over in the majority of states) must be filed in the state or territory's Supreme Court. If a claim involves bankruptcy or corporate insolvency, or if it includes statutory claims under federal law, it may be filed in the Federal Circuit Court or the Federal Court.

**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 schemes of arrangement, when it is necessary to employ a trained insolvency practitioner as an advisor. It is pertinent to note here that 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.

This answer is far too long and does not address the question that was asked. I have awarded marks for the issues that were raised that are correct.

**QUESTION 4 (fact-based application-type question) [15 marks in total]**

**Commented [DB5]:** 6 out of 15

**Question 4.1 [maximum 8 marks] 3 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 in both Sydney and in Lyonesse. Its warehouses are only in Sydney. Aussiebee regularly sells its chocolates all over the world, with orders received in Lyonesse and shipped from the Sydney 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 under the *Cross-Border Insolvency Act 2008*, 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]

**Advice:**

ATO can consider adopting the following measure to improve and/or protect its position:

A. **ATO can institute proceeding against the Directors of Aussiebee: intervene on the recognition application?**

**In Australia a director is liable for insolvent trading where he or she was a director at the time a debt was incurred. However, in an attempt to reduce the stifling effect of the insolvent trading provisions on business rescue attempts, a "safe harbour" provision was introduced with effect from September, 2017. The safe harbour provisions provide that insolvent trading liability is not incurred where, after the time that directors begin to suspect the company may be or may become insolvent, they start developing one or more courses of action that are reasonably likely to lead to a better outcome for the company. However, it is pertinent to note that the safe harbour only applies if all the following conditions are fulfilled:**

- **to debts incurred directly or indirectly in connection with the proposed course of action, including ordinary trade debts incurred in the usual course of business or debts taken on for the specific purpose of effecting the plan;**
- **if the company continues to pay all employee entitlements (including superannuation) as and when they fall due; and**
- **if the company continues to comply with all tax reporting obligations**

Since in the instant case the Company failed to comply with its tax obligations. It shall not attract the Safe Harbour provision and accordingly, the ATO can institute the proceeding against the Director of the Debtor (Aussiebee); especially those who are also the National of Australia.

B. **Initiation of proceeding for Recognition of Order**

The ATO can apply to the Court for recognition order in the proceeding instituted by the Aussiebee's Liquidator and enforcing there claims in Austraila, 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 in Lyonesse.

As has been held in the case of Ackers vs. Deputy Commssioner of Taxation where a company owed over AUD 83 million in tax and penalties in Australia. Since, a debt payable to a foreign revenue creditor is not admissible to proof in a Cayman Islands liquidation. The Deputy Commissioner of Taxation (DCT) applied for permission to enforce its claim in Australia, expressly for the purpose of recovering an amount up to pari passu amount.

This has not been well answered. This is what you should have said:

The ATO should intervene on the recognition application, arguing that:

- The COMI of Aussiebee is Australia, not Lyonesse, and so the assets of Aussibee should not be entrusted to the Lyonessian liquidator.
    - *Ackers v Saad Investments* is the leading Australian decision on COMI. It followed and expressly adopted the principles in *Re Eurofoods IFSC Ltd* that COMI is to be determined having regard to the objectively ascertainable factors of the debtor.
    - Need to displace presumption that place of incorporation is COMI
    - Six of the seven directors are Australians
    - The CEO is Australian (although resident in Lyonesse)
    - The CFO is Australian and resident in Australia
    - Sells Australian product, manufactured by its subsidiary in Australia, shipped from 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.

Applying *Ackers v Deputy Commissioner of Taxation*, that if the Court is to entrust the NewYums shares to the Lyonessian liquidator, then the ATO should give leave to the ATO to take steps to enforce its claim in Australia, expressly for the purpose of recovering an amount up to the pari passu amount the ATO would have received if it were entitled to prove for the tax debt as an unsecured creditor in the Lyonessian proceeding, because this is an appropriate way to ensure that the interests of the ATO as a creditor were adequately protected (Model Law, Art 22).

**C. Issue a director Penalty Notice**

The amendments made in February 2020 permit the Commissioner of Taxation to keep any tax refund due to a firm if the company has neglected to file a late tax return or provide the Australian Taxation Office with any unfinished business.

**D. Direction as per Rizzo-Bottiglieri-de Carlini Armatori decisions:**

As has been held in the case of Rizzo-Bottiglieri-de Carlini Armatori by federal court of Australia for recognition of an Italian fallimento proceeding, that the 'serious lacuna' in relation to Article 18(a) of the Model Law, whereby the former

foreign representative has no incentive to inform a recognising court of the termination of a foreign proceeding, with the result that Australian stays will remain in force long after the relevant foreign proceeding has been terminated. The process for determining which of the Australian stays should apply to a recognised foreign main proceeding: the voluntary administration stay which affects secured creditors or the liquidation stay which does not affect secured creditors. The correct stay to apply is determined by the nature of the proceeding and whether it is more analogous to an Australian voluntary administration or a liquidation.

Thus, the ATO can request the Federal Court of Australia before which the stay is requested to either with the recognition application pay into court an amount by way of security only recoverable on an application under Article 18 or make stay orders under Article 19, 20 or 21 for a fixed period of 3 months and to require the Aussiebee's Liquidator to report to the Court at regular interval.

**Question 4.2 [maximum 7 marks]** 3 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.

A competitor has recently approached HA with an attractive offer to purchase the 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]

**Issues to be addressed:**

- **Issue I : Possibility of Formal Insolvency Process being instituted against the Creditor**

- **Advice to the Board:**

    - Since in the instant case the HA has to pay AUD 4.6 million in damages to BOR as well as have a AUD 3 million loan from CBA. Along with borrowings from its Parent Company HGL. Thus, it falls outside the scope of a restructuring process and restructuring plan under the new Part 5.3B of the Corporations Act which came into effect on 1 January 2021 for small enterprises with liabilities of less than AUD million.
    - Thus, there are two, types of formal corporate rescue in Australia:
        - voluntary administration, followed by the implementation of a deed of company arrangement
        - a creditors' scheme of arrangement
    - A company cannot be wound up under section 459C of the Corporations Act unless it is insolvent. If a firm doesn't comply with a statutory demand during the three months prior to the filing of an application to wind it up, it will be assumed to be insolvent. Thus, considering the foreseeable Demand Notice from BOR, the Board should immediately start taking steps to ensure liquidity of funds.

- **Issue II: Safe Harbour Clause and subsequent right that emerges in favour of HGL:**

- **Advice to the Board:**

    - In the instant case if the formal insolvency process against HA is initiated a liquidator (or ASIC) may pursue a director for insolvent trading under section 588G of the Corporations Act, or a holding company under the equivalent provision in section 588V of the Corporations Act. In practice, Australia's insolvent trading laws have until recently been regarded as being among the harshest in the world, with limited defences available and directors previously unable to avoid personal liability if they caused a company to incur a debt in pursuit of a genuine restructuring attempt.
    - However, the safe harbour from insolvent trading provides a new means for directors to avoid personal liability for insolvent trading in circumstances where they pursue a restructuring attempt under the advice of a specialist restructuring expert and the company has a realistic prospect of being able to trade out of its current financial difficulties. That said, the safe harbour should not be seen as any kind of guaranteed immunity for directors, who must remain actively involved in the development of a restructuring plan and diligently monitor the company's financial performance to be able to invoke the carve-out to personal liability.

- **Issues III: Issues of BGL Loan to be declared an Unfair Transaction:**

- **Advice to the Board:**

    - A liquidator may resort to the voidable transaction provisions of the Corporations Act to recover dispositions of property by a company which are unfair preferences, uncommercial transactions, unreasonable director-related transactions or unfair loans. A loan is deemed to be “Unfair” under the Corporation Act if the interest or charges in relation to the loan are or at any time have been extortionate. This is precisely relevant in the istant case as the funding for the Perth plant has been provided by HGL as an unsecured loan for AUD 30 million as well as additional borrowing of AUD 5 million. Thus, a due diligence in this regard is essential to safeguard the rights of HGL.

- **Issues IV: Issues of unfair preference and uncommercial transactions:**

- **Advice to the Board:**

    - The unfair preference and uncommercial transactions provisions are only able to recover property if a transaction was entered into at the time the company was insolvent or otherwise caused the company to become insolvent. Since in the instant case a competitor has recently approached HA with an attractive offer to purchase the Perth re-refining plant. It is clear and evident that there does not exist any directors personal insolvency.

- However, before the said transaction is executed, as a precautionary thorough inspection and due diligence of the related party with the competitor should be undertaken, to avoid it being an unreasonable director-related transactions or an uncommercial transaction. In this regard the following defences are available with the Board:
  - Acted in good faith:
    Since the HGL in the instant case is acting in good faith and for the benefit of the Creditors at large aiming to maximise the value of the assets and restructure the firm. Furthermore, it is pertinent to note that HA is already insolvent. Hence, vide the instant transaction measures are being taken to rescue the Business
  - Provided Valuable/Adequate Consideration:
    The consideration so availed from the Competitor is adequate and as per prevailing market value and not under or at discounted rates.

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- **Issues V: Enforcement of Security Interest by CBA**

- **Advice to the Board:**

  - CBA being the Secured Creditor and thus, would have priority in repayment if the formal liquidation proceeding begins if their mortgages would have been registered on the Personal Property Securities Register. Since in the instant case the Security interest over personal property is non-circulating i.e., they are granted over the three (3) trucks. AS perfection by way of registration is critical to the protection of the secured creditors rights in insolvency. However, it being an unperfected security interest will automatically vest in the favour of Debtor i.e. HA unless the security interest gets registered 6 months prior to the initiation of the external administration.

- **Issues VI: Safeguarding HGL from Insolvency Proceeding**

- **Advice to the Board:**

  - The amendments introduced in 2019 were aimed at deterring directors from attempting to avoid paying the company's employees in an insolvency context. Thus, vide this amendment the Court has a power to make an "employee entitlements contribution order" against a parent company or any other entity which has benefited from the services of the employees of a company being liquidated. Since the scope of such order is limited to employees, it is essential that such creditors are paid as and when the dues arise to avoid such an obligation being transferred to the parent company i.e. HGL.

Your answers are too long and do not focus on the issues at play. The answer to this question was as follows:

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 $30m loan will not be due and payable during the voluntary administration, because of the *ipso facto* clause moratorium. But the *ipso facto* clause can and will operate once the company executes a DOCA or goes into liquidation.

- 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 PPSA. Unperfected (ie unregistered) interests vest in the voluntary administrator immediately before the commencement of a voluntary administration (*Personal Property Securities Act*, s 267). The voluntary administration can then sell the trucks to provide a return to unsecured creditors.

- The VAs, or HGP, could propose a DOCA, involving the sale of the Perth plant and the sale proceeds going into a fund to pay unsecured creditors.

- 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.

Liquidation would be risky, because:

- HGL is exposed to holding company insolvent trading liability

- As directors of HA, they are personally exposed to insolvent trading liability.

Exposure is for all debts incurred whilst insolvent.

*** End of Assessment ***