



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 202223-336.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 dealing 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 2023**. The assessment submission portal will close at 23:00 (11 pm) BST (GMT +1) on 31 July 2023. 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 **9 pages**.

ANSWER ALL THE QUESTIONS

Commented [BB1]: TOTAL = 45.5/50 (91%)

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

Commented [BB2]: Sub-total = 10 marks

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.

Question 1.2

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

- (a) Small company restructuring.
- (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.
- (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.

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.

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.

(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.

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.

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

(d) A safe harbour from insolvent trading liability.

MULTIPLE CHOICE: 10/10

QUESTION 2 (direct questions) [10 marks]

Commented [BB3]: Sub-total = 8.5 marks

Question 2.1 [maximum 3 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.

Answer:

In Australia, under Part 5.7B of the Corporations Act, 2001 certain type of transactions may be held to be void and set aside after a company has entered into liquidation. The detail of the same¹ along with defence available to the opposite party is as under²:

Sl. No	Type of the transaction	Details	Defence available
I.	Unfair preferences	<p>Unfair Preferences are the most common type of voidable transaction and occurs where a creditor has received an advantage over other creditors, by receiving payment (or other type of transaction) for their outstanding liabilities and does so in circumstances where they knew, or ought to have known, that the company was insolvent.</p> <p>To be set aside, an unfair preference must occur at a time:</p> <ul style="list-style-type: none">• within six months of the 'relation back day'.• in the four-year period ending on the relation back day where the creditor is a related entity of the company.• in the 10-year period ending on the relation	<p>The other party to the transactions prevents it from being held void if it can be proved that³:</p> <p>(i) they became a party in good faith;</p> <p>(ii) they lacked reasonable grounds for suspecting that the company was insolvent or would become insolvent by entering into the transaction; and</p> <p>(iii) they provided valuable consideration or changed their position in reliance on the transaction.</p>

¹ SV Patners. (2023, June 17). What is a voidable transaction? Retrieved from SV Patners: <https://svpartners.com.au/resource-centre/voidables/guide-to-corporate-voidable-transactions/>

² Cho, L. A. (2023, June 17). *What Are Voidable Transactions?* Retrieved from Legal vision: <https://legalvision.com.au/what-are-voidable-transactions/>

³ Global Restructuring Review. (2023). *Restructuring & Insolvency in Australia*. United Kingdom: Lexology.

		<p>back day where the transaction was entered into for a purpose which included defeating, delaying or interfering with the rights of creditors in the event of insolvency.</p> <ul style="list-style-type: none"> • after the relation back day but on or before the liquidator was appointed.
II.	Uncommercial transactions	<p>An uncommercial transaction relates to transactions entered into by a company where it may be expected that a reasonable person in the company's circumstances would not have entered into the transaction, by having regard to its benefits and/or detriments to the company.</p> <p>If a company enters into a transaction with any person (not just a creditor) in circumstances where the transaction:</p> <p>(i) occurred at a time:</p> <ul style="list-style-type: none"> • in the two-year period ending on the relation back day. • in the four-year period ending on the relation back day where the other person is a related entity of the company. • in the 10-year period ending on the relation back day where the transaction was entered into for a purpose which included defeating, delaying or interfering with the rights of creditors in the event of insolvency. • after the relation back day but on or before the liquidator was appointed. <p>(ii) occurred when the company was insolvent or otherwise caused the company to become insolvent;</p>
III.	Unreasonable director-related transactions	An unreasonable director-related transaction arises when a

		<p>transaction is entered into by a director or close associate of the company, in circumstances where it may be expected that a reasonable person in the company's circumstances would not have entered into the transaction. Liquidator can apply to the court to challenge an unreasonable director-related transaction of the company if it was entered into during the four years ending on the relation back day, or after that day but before the liquidator was appointed.</p>
IV.	Unfair loans	<p>Unfair Loans may arise in circumstances where a loan to a company is unfair and meets either of the following tests (as set out in s 588FD of the Corporations Act 2001 (Cth)):</p> <p>The interest on the loan was extortionate when the loan was made, or has since become extortionate because of a variation; or the charges in relation to the loan were extortionate when the loan was made, or have since become extortionate because of a variation, even if the interest is, or the charges are, no longer extortionate.”</p> <p>A liquidator making a claim to a court under s 588FF of the Corporations Act 2001, for an unfair loan need not determine whether the company was insolvent at the time of entering into the loan and the claim depends upon the circumstances and facts of the case. For a liquidator to successfully bring an unfair loan claim against a lender, the liquidator must show that the events leading up to, and during, the entering into the loan arrangement, the lender extorted the borrower.</p>
V.	Circulating security interests	<p>Circulating security interests (formerly floating charges) created within six months before</p>

		<p>the commencement of liquidation and securing past indebtedness are void against the liquidator, unless the company was solvent immediately after granting the security. Not only is the circulating security interest itself void, but the liquidator may also bring court proceedings to recover the proceeds of any realisation of the void circulating security interest. However, this provision only applies in compulsory liquidations on grounds of insolvency.</p> <p>Circulating security interest is deemed by the Corporations Act to be void against the liquidator if it has been created in the six-month period before the commencement of the external administration and the secured creditor has not provided new value (such as new goods or services) as consideration for taking the security interest.</p>	
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QUESTION 2.1: 2.5/3

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?

Answer:

The Cross-border Insolvency Act 2008 (the CBIA) gives the force of law in Australia to the UNCITRAL Model Law on Cross-border Insolvency (Model Law). Under the Model Law, a 'foreign representative' can apply to the Federal Court of Australia or the Supreme Court of a state or territory to have a foreign insolvency proceeding recognised in Australia as a 'foreign main proceeding'. Several consequences flow from recognition, perhaps the most important of which is an automatic stay of actions or proceedings in Australia concerning the debtor's assets, rights, obligations or liabilities. 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."

Accordingly, when an Australian court is considering a recognition application in relation to a corporate debtor, it needs to consider what "the case requires", that is, whether the case requires the broader voluntary administration stay which affects secured creditors or the standard liquidation stay that affects only unsecured creditors. ***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. In this case it was decided that granting a stay is not a question of discretion but rather which stay should apply will be decided according to the nature of the foreign proceeding⁴.

It may be further noted that where the foreign proceeding is clearly a business rescue procedure, the broader voluntary administration stay will be more appropriate. The voluntary administration stay will be more appropriate for foreign proceedings that are more analogous to liquidations.

QUESTION 2.2: 3/3

Question 2.3 [maximum 4 marks]

What are the differences between liquidations and small company liquidations?

Answer:

As of 1st January 2021, there will be two different forms of creditors' voluntary liquidation (CVL), the normal version and a simplified version for small companies. The major differences⁵ between the two is as under:

Key Consideration	Creditors Voluntary Liquidation (CVL)	Simplified Liquidation Process (SLP)
Eligibility	Accessible to all companies	Available if commenced on or after 1 Jan 2021 and eligibility criteria met, which primarily includes, but is not limited to: <ul style="list-style-type: none"> • Liability test: <\$1 million • No prior Small Business Restructurings or SLPs by company or any directors (7yr threshold) • All tax lodgements up to date
Who can appoint?	a. Members can resolve to wind up and appoint a liquidator. b. Creditors can resolve to wind up at the conclusion of Voluntary Administration or if Deed of Company Arrangement fails. c. ASIC	The liquidator may adopt SLP within the first 20 business days only after CVL commences a. Creditors & members must be given 10 business days' notice of intention to adopt. b. As long as no more than 25% of creditors by \$ value objected to the adoption.
Control of Company	Liquidator assumes control and is an "officer" of the company	<ul style="list-style-type: none"> • Liquidator continues control and is an "officer" of the

⁴ Abernethy, D., Salman, J., & Sutherland, K. (2016, December 14). *Australia: To stay or not to stay? Stay and suspension of enforcement proceedings in cross border insolvencies*. Retrieved from Mondaq: <https://www.mondaq.com/australia/international-trade-investment/552714/to-stay-or-not-to-stay-stay-and-suspension-of-enforcement-proceedings-in-cross-border-insolvencies>

⁵ Australian Securities and Investments Commission (ASIC). (2023, June 17). Simplified liquidation. Retrieved from Australian Securities and Investments Commission (ASIC): <https://asic.gov.au/regulatory-resources/insolvency/insolvency-for-directors/simplified-liquidation/>

		<p>company.</p> <ul style="list-style-type: none"> • Creditors lose power to replace the appointee. • No reviewing of liquidators unless review enforced by the Court.
Meetings of creditors	<p>No requirement to have a meeting of creditors, but if a certain number/dollar value of creditors require it, the liquidator can be compelled to convene one.</p> <p>Liquidator has discretion to convene a meeting at any time.</p> <p>Committee of Inspection may be formed.</p>	<p>No meetings permitted (therefore, creditors power to request a meeting now redundant).</p> <p>No Committee of Inspection permitted.</p>
Scope of debts covered	<p>All unsecured debts, including priority employee entitlements.</p> <p>Secured creditors only affected to the extent there is a shortfall in their security</p>	<p>All unsecured debts, including priority employee entitlements.</p> <p>Secured creditors only affected to the extent there is a shortfall in their security</p>
Extent of costs involved	<p>Dependent on company and complexity, but generally higher due to non-streamlined process.</p> <p>Typically calculated on a time cost basis which is subject to approval.</p>	<p>Dependent on company and complexity, but generally lower due to streamlined process.</p>
Timeline	<p>Dependent on company and complexity.</p> <p>Complex litigation, for example pursuing recoveries for the benefit of creditors most likely contributor to delays.</p>	<p>Dependent on company and complexity.</p> <p>SLP may be required to cease in specified circumstances, in which case the winding up reverts back to a normal CVL (however this may not impact the timeline).</p>
Investigating & Reporting	<p>Obligation to investigate the affairs of the company – this may reveal legal recovery actions which benefit creditors (e.g. insolvent trading).</p> <p>Misconduct (if found) must be reported to ASIC (s533 of the Corporations Act).</p> <p>Only one statutory report to creditors required, but discretion to report further should circumstances warrant it.</p> <p>ASIC lodgements of documents and forms.</p>	<p>Same as CVL except:</p> <ul style="list-style-type: none"> • Misconduct report (s533) not required unless serious, material misconduct, therefore reduced investigation obligations. • Simplified statutory report to creditors. <p>ASIC lodgements of documents and forms</p>
Enforcement of Claw back	<p>Full range of recoveries include unfair preferences, unreasonable director – related transactions, creditor defeating transactions and</p>	<p>Full range of recoveries are still available. However, the definition of unfair preferences has been narrowed to a 3-month relation back</p>

	insolvent trading	date (instead of 6 months) and total value of targeted transactions must be ≤\$30 000 (no limit in a normal CVL)
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QUESTION 2.3: 3/4

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

Commented [BB4]: Sub-total = 15 marks

“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.

Answer:

The statement suggests that recent reforms in Australia have shifted the balance of insolvency and restructuring laws to be more favourable towards debtors rather than creditors. To critically discuss this statement, let’s examine both sides of the argument:

Creditor-Friendly Perspective:

Australia’s insolvency regime, for both personal and corporate debtors, is regarded as being creditor-friendly. The primary focus is on the protection of creditors’ rights to the exclusion of management and shareholders, notwithstanding the consequent adverse impact on corporate and business rescue which may be in the interests of employees, small suppliers and other corporate stakeholders. The Australian insolvency law provide the following rights to the Creditors:

(i) Enforcement of rights by Secured Creditors: Secured creditors are entitled to enforce their rights during the bankruptcy process for an insolvent individual and they are not bound by the bankruptcy moratorium⁶. If a secured creditor realises its security and there is a shortfall, the secured creditor may submit a proof of debt for the shortfall. In addition to this under the liquidation process for an insolvent company moratorium applies only to unsecured creditors and not to secured creditors⁷ and they are permitted to enforce any rights that they have under any valid security interest.

(ii) Maximum return to the Creditors: Despite one of the stated aims of voluntary administration (as the primary formal corporate rescue process in Australia) being to maximise the chance of an insolvent company, or as much as possible of its business, continuing in existence under the terms of a deed of company arrangement (DOCA),⁸ an alternative aim of voluntary administration as per the Corporations Act is to simply enable a maximum return to be achieved for distribution to creditors.

(iii) Power to appoint receiver in voluntary administration: A creditor with a security interest over the whole, or substantially the whole, of a company’s property – in that case, the creditor can enforce its security interest, typically by appointing a receiver, within the “decision period” of 13 business days from the commencement of the voluntary

⁶ S 58(5) of Bankruptcy Act.

⁷ S 471C of Corporation Act.

⁸ S 435A(a) of Corporations Act.

administration or from the secured party receiving notice of the appointment of the voluntary administrator⁹.

(iv) Continuation of enforcement action during voluntary administration: Major secured creditors, as well as owners and lessors with enforcement rights, can continue with enforcement action which has been commenced prior to the appointment of a voluntary administrator or which relates to perishable property, or otherwise with the consent of the court¹⁰.

(v) Insolvent Trading liability upon Directors: Australia has broad insolvent trading liability, which allows a liquidator to recover substantial sums from directors (usually via a directors' and officers' insurance policy) where the directors have allowed a company to incur debts whilst insolvent;

(vi) Strong voidable transaction regime: Australia's voidable transaction regime¹¹, particularly in corporate liquidation, allows transactions to be clawed back for the benefit of creditors over a substantial period of years and without having to prove improper conduct such as an intention to defeat creditors.

(vii) Priority of payment: Australia has established a clear and hierarchical order of priority for creditor repayment in insolvency proceedings. Secured creditors and certain priority creditors, such as employees, generally have preferential rights to be paid before unsecured creditors.

Debtor-Friendly Perspective:

The recent reforms to the corporate insolvency process in Australia are designed to encourage a stronger corporate and business rescue culture and promote a move away from the existing dominance of creditors' rights. The details of the same is as under:

(i) Focus of rescue: The voluntary administration regime has as its primary goal the maximisation of the chance of an insolvent company, or as much as possible of its business, continuing in existence under the terms of a DOCA¹². In an important recent decision of *Mighty River International Ltd v Hughes (2018) 265 CLR 480* the High Court of Australia emphasised the primary intended use of voluntary administration to achieve corporate or business rescue, approving a "holding DOCA" underpinned by an ongoing moratorium on the enforcement of creditors' claims and no interim distribution of dividends to creditors while the deed administrator pursued means of saving the company or achieving a going concern sale of its business. This highlights the fact that rescue of company is given more importance than protecting the rights of the Creditors.

(ii) Prohibitions on enforcement of claims by creditors: The Corporations Act 2001 imposes an automatic stay on the enforcement of ipso facto clauses in certain contracts entered into on or after 1 July 2018¹³. The automatic stay applies where one of the following insolvency events occurs in relation to a company:

- voluntary administration;

⁹ S 441A of Corporation Act.

¹⁰ S441D, 441H of Corporation Act.

¹¹ Section 588G of the Corporations Act.

¹² S 435A(a) of Corporations Act.

¹³ Baker McKenzie. (2020). The "Ipso Facto" prohibition in the Corporations Act applicable to Corporate Insolvency. Sydney: Baker & McKenzie.

- a receiver or controller is appointed over the whole or substantially the whole of the company's assets;
- the company announces, applies for or becomes subject to a scheme of arrangement to avoid a winding up; or the appointment of a liquidator immediately following an administration or a scheme of arrangement.

The scope of the automatic stay, specifically what contract types, rights and self-executing provisions are excluded by the automatic stay are set out in the Corporations (Stay on Enforcing Certain Rights) Regulations 2018 (the Regulations) and the Corporations (Stay on Enforcing Certain Rights) Declaration 2018 (the Declaration). Further, the personal insolvency regime takes an even stricter approach, with the Bankruptcy Act rendering ipso facto clauses void outright when a person becomes bankrupt¹⁴.

(iii) Safe Harbour Provision: Australia introduced a safe harbour provision in 2017, which provides directors with protection from personal liability for insolvent trading if they take reasonable steps to turn around the company and avoid insolvency¹⁵. Accordingly, a director will not be liable for debts incurred by a company while it is insolvent if, 'at a particular time after the director starts to suspect the company may become or be insolvent, the director starts developing one or more courses of action that are reasonably likely to lead to a better outcome for the company' than the 'immediate appointment of an administrator or liquidator to the company'.

(iv) New small company restructuring process: Recently, the Australian Government has introduced a New small company restructuring process to enable financially distressed small companies to restructure their existing debts. The object of the restructuring process is for companies to retain control of their business, property and affairs while developing (with the assistance of a restructuring practitioner) a restructuring plan¹⁶.

Conclusion:

It is important to note that while recent reforms have introduced some debtor-friendly provisions, Australia's insolvency and restructuring framework continues to emphasize the importance of creditor rights and the orderly distribution of assets. The reforms aim to strike a balance between the interests of debtors and creditors, recognizing the need for economic growth and the preservation of viable businesses while protecting creditor interests.

Whether Australia's insolvency and restructuring options have become more debtor-friendly or creditor-friendly is subjective and can depend on individual perspectives. The reforms have sought to address certain challenges faced by financially distressed companies, particularly small businesses in wake of Covid-19, while still maintaining important creditor protections and upholding the principles of insolvency law.

Hence, it can be concluded that recent reforms in Australia have introduced debtor-friendly provisions, but they have not fundamentally shifted the jurisdiction to be solely debtor-friendly. The insolvency and restructuring framework in Australia continue to maintain a balance between debtor rehabilitation and creditor rights, reflecting the need for a fair and effective resolution of financial distress.

¹⁴ S 301 Of the Bankruptcy Act.

¹⁵ S 588GA of the Corporation Act

¹⁶ Corporations Amendment (Corporate Insolvency Reforms) Act 2020, cl 452A(a).

15/15 marks – very strong essay. Identifies every relevant process for both camps (including recent reforms which favour the rights of debtors). Strong analysis and summary of the major aspects of Australia's insolvency process.

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

Commented [BB5]: Sub-total = 12 marks

Question 4.1 [maximum 8 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 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 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 Lyonessean liquidation.

Aussiebee owes AUD 12 million in taxes in Australia, payable to the Australian Taxation Office (ATO). Assume that revenue creditors such as the ATO are not entitled to prove in the Lyonessean liquidation.

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

Answer:

It is understood from the fact of the case that Aussiebee owes AUD 12 million in taxes in Australia, payable to the Australian Taxation Office (ATO). Further, assumption is provided that revenue creditors such as the ATO are not entitled to prove in the Lyonessean liquidation. Considering these circumstances as an adviser to the ATO, I will advise him to take the following steps to protect or improve its position:

(i) Challenging centre of main interests (COMI): A main proceeding is one taking place where the debtor had its centre of main interests (COMI) at the date of commencement of the foreign proceeding. In principle, a main proceeding is expected to have principal responsibility for managing the insolvency of the debtor regardless of the number of States in which the debtor has assets and creditors, subject to appropriate coordination procedures to accommodate local needs. COMI is not defined in the Model Law, but is based on a presumption that it is the registered office or habitual residence of the debtor. Australia formally adopted the UNCITRAL Model Law on Cross-Border Insolvency by implementing the Cross-Border Act. Under the Cross-Border Act, there is a rebuttable presumption that the centre of the debtor's main interest is its registered office, or in the case of a natural person, his or her habitual residence. In considering where the COMI of a debtor or group of companies exists, the courts will look at a number of factors, including:

- the location of the debtor's headquarters;
- the location of those who actually manage the debtor;
- the location of the debtor's primary assets;
- the location of the majority of the debtor's creditors or a majority of creditors who would be affected by the case; and
- the jurisdiction whose law applies to most disputes.

In the instant matter since Aussiebee has its one office in Sydney and its warehouses are only in Sydney. Further its board of directors, made up of six Australians and one Lyonesian while its CFO is an Australian, resident in Australia. First step that ATO can take is it can request court to recognise Lyonesian foreign proceeding as non-main proceeding. This will ensure that future proceeding in Australia will be recognised as main proceeding and ATO rights will be protected as per Australian law.

(ii) Filing an application with the Federal Court seeking relief under, relevantly, Article 22.3 of the Model Law: The ATO may file an application with the Federal Court seeking relief under, relevantly, Article 22.3 of the Model Law. Article 22.3 of the Model Law provides that *"The court may, at the request of the foreign representative or a person affected by relief granted under article 19 or 21, or at its own motion, modify or terminate such relief"*. Accordingly, the ATO may sought to modify the recognition orders (if recognised as main proceeding) so as to prevent the liquidators from realising the Australian assets for the benefit of creditors in the Lyonesian liquidation. The basis of the application will be that the ATO, being revenue creditors are not entitled to prove in the Lyonesian liquidation.

(iii) Seeking protection of interest under article 22.1 of the Model Law: The fact of the case indicates that ATO, being a foreign revenue creditor, would have its proof rejected. Accordingly, ATO may argue that such an outcome will be unfair. Accordingly, it can be pleaded that the Australian Court should provide the ATO with 'adequate protection' within the meaning of Article 22.1 of the Model Law. Article 22.1 of the Model Law states that *"In granting or denying relief under article 19 or 21, or in modifying or terminating relief under paragraph 3 of this article, the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected"*. It can be further argued that this would be achieved by making provision for the ATO from Aussiebee Australian assets in an amount equivalent to that which the ATO would have received if its proof were able to be admitted in the Cayman Islands.

(iv) Seeking restriction on liquidators' authority to remit Aussiebee Australian assets to the Lyonesse and permitting the ATO to take recovery action against Aussiebee Australian assets: The ATO would be unable to receive any dividend from the Lyonesian liquidation proceeding and this would produce a windfall gain for other creditors and Aussiebee would benefit from its insolvency by avoiding tax. According, ATO can argue that this was inconsistent with the proper and fair distribution to creditors of a cross-border insolvent; an objective of the Model Law. Further ATO can seek restriction on liquidators' authority to remit Aussiebee Australian assets to the Lyonesse and permitting the ATO to take recovery action against Aussiebee Australian assets. This recovery action would include the issuing of statutory notices under Commonwealth tax legislation.

(v) Relevant Case law: The ATO can rely on case of ***Ackers v Deputy Commissioner of Taxation (2014) 223 FCR 8; [2014] FCAFC 57*** wherein on an application of the Deputy Commissioner of Taxation (DCT), the Federal Court modified the recognition orders, giving leave to the DCT 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 they

were entitled to prove for the tax debt as an unsecured creditor in the foreign main proceeding. On appeal, the Full Court upheld the decision, finding that the modification of the recognition orders was an appropriate way to ensure that the interests of the DCT as a creditor were adequately protected.

8/8 marks – exemplar answer. Addresses all of the relevant substantive law and applies it correctly to the facts of the question. Comes to the right conclusion regarding the COMI and the correct conclusions regarding a pari passu amount equivalent to that which the ATO would have received if it were an unsecured creditor in the Lyonessian proceeding.

Question 4.2 [maximum 7 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?

Answer:

As an Advisor to the Board, I will highlight the different types of liquidation and formal corporate rescue procedure available in Australia, considering the circumstances of the case.

A. Corporate liquidation:

(i) Creditors' voluntary liquidation: Under a creditors' voluntary liquidation, a liquidator can be appointed:

- by special resolution of shareholders if the directors believe the company is insolvent. The liquidator must then convene a meeting of creditors within 10 business days, with creditors given the power to replace the liquidator, request information and reports and / or appoint a committee of inspection; or
- if resolved by creditors at the second meeting of creditors held during voluntary administration.

B. Corporate Rescue Procedure:

(i) Voluntary administration, followed by the implementation of a DOCA (deed of company arrangement) under Part 5.3A of the Corporations Act

The voluntary administration procedure in the Corporations Act was introduced in 1993. The primary objective of voluntary administration is to provide for the business, property and affairs of an insolvent company to be administered in a way that:

- maximises the chances of the company, or as much as possible of its business, continuing in existence; or
- if it is not possible for the company or its business to continue in existence – results in a better return for the company's creditors and members than would result from an immediate winding up of the company.

The voluntary administration process gives a company a short breathing space, during which there is a general moratorium on the enforcement of creditors' claims. It enables the administrator to continue to trade the company's business during the administration period, and for any proposal to rehabilitate the company or otherwise maximise returns to creditors (other than via an immediate winding up) to be put before creditors and, if approved, implemented via a deed of company arrangement (DOCA). A DOCA will be binding on key stakeholders including the company, its shareholders and its creditors (save for secured creditors who do not vote in favour of the DOCA). The DOCA is generally proposed by the director or any third-party, usually in consultation with the voluntary administrator, and is administered by a deed administrator (usually the registered liquidator who was the voluntary administrator).

(ii) Creditors' scheme of arrangement under Part 5.1 of the Corporations Act

A scheme of arrangement is a restructuring tool that sits outside of formal insolvency. The company may become subject to a scheme of arrangement whether it is solvent or insolvent. A scheme of arrangement is a proposal put forward (with input from management, the company or its creditors) to restructure the company in a manner that includes a compromise of rights by any or all stakeholders. The process is overseen by the courts and requires approval by all classes of creditors. The pre-existing management retains control of the company during the process (and also depending on the terms of the scheme itself after its implementation).

A scheme of arrangement must be approved by at least 50 per cent in number and 75 per cent in value of creditors in each class of creditor. It must also be approved by the court to become effective. The outcome of a scheme of arrangement is dependent on the terms of the arrangement or compromise agreed with the creditors, but most commonly, upon implementation, a company is returned to its normal state as a going concern but with the relevant compromises having taken effect.

The choice of insolvency process will depend on the specific circumstances and other relevant factors to be considered by the Board. Main issues that the board of HGL and HA should be aware of in light of the facts set out above in the case is highlighted as under:

(i) Loss of unregistered personal property security: The fact of the case indicates that HA owns three large trucks which 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. However, the mortgages are not registered on the Personal Property Securities Register (PPSR). Accordingly, the failure to register or otherwise perfect a security interest can cause the loss of the security on insolvency. Any unperfected security interest will automatically vest in the grantor (usually the debtor) immediately prior to the commencement of a bankruptcy, voluntary administration or liquidation of the grantor.

(ii) Ipso facto moratorium: The Corporations Act 2001 imposes an automatic stay on the enforcement of ipso facto clauses in certain contracts entered into on or after 1 July 2018. The automatic stay applies where one of the following insolvency events occurs in relation to a company:

- voluntary administration;
- a receiver or controller is appointed over the whole or substantially the whole of the company's assets;
- the company announces, applies for or becomes subject to a scheme of arrangement to avoid a winding up; or the appointment of a liquidator immediately following an administration or a scheme of arrangement.

The scope of the automatic stay, specifically what contract types, rights and self-executing provisions are excluded by the automatic stay are set out in the Corporations (Stay on Enforcing Certain Rights) Regulations 2018 (the Regulations) and the Corporations (Stay on Enforcing Certain Rights) Declaration 2018 (the Declaration). Accordingly, **Board may check whether loan granted by HGL to HA is covered Ipso facto moratorium and loans does not becomes automatically due and payable in full due to entry of HA IN to any formal insolvency or restructuring process in Australia.**

(iii) Safe Harbour Provisions: Before the introduction of the safe harbour Section 588GA of the Corporations Act, states directors of a company would typically appoint a voluntary administrator at the first sign of financial trouble in an attempt to avoid personal liability for insolvent trading (by invoking the defence to liability under section 588H(6) of the Corporations Act). However, with the introduction of this 'safe harbour'¹⁷ from insolvent trading liability is likely to encourage directors to pursue an informal restructuring attempt acting on the advice of a restructuring expert where the company, despite existing financial difficulties, is likely to be able to trade out of those difficulties in the longer-term

(iv) Future prospects of the Company: The Board needs to consider whether the company has any realistic prospects of becoming profitable again. This will help in deciding the type of liquidation and formal corporate rescue procedure to be opted by the Board.

¹⁷ Section 588GA of the Corporation Act

(v) Evaluate Sale of Assets: Assess the offer from the competitor interested in purchasing the Perth re-refining plant. Consider whether the sale proceeds could be used to address the company's debts or provide a better outcome for creditors compared to other alternatives.

(vi) Explore Negotiations and Restructuring: Engage in discussions with creditors, including the CBA and BOR, to explore potential restructuring options. This may involve negotiating repayment terms, seeking a reduction in the damages owed, or entering into alternative payment arrangements.

Accordingly, above issues may be considered by the Board before taking decision about the future of the Company.

QUESTION 4.2: 4/7

*** End of Assessment ***