



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 = 46/50 (92%)

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 = 9 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.

The five types of voidable transactions that can be reversed by a liquidator on application to the court are:

- *unfair preferences;*
- *uncommercial transactions;*
- *unreasonable director-related transactions;*
- *unfair loans; or*
- *circulating security interests (in limited circumstances)*

Concerning unfair preferences and uncommercial transactions, the Corporations Act contains a limited defence. The defendant must prove that he or she was not aware that the company was insolvent at the time he or she entered into the transactions. But also, the defendant must demonstrate that he or she acted in good faith and provided valuable consideration or changed its position in reliance on the transaction. In other words, it is not a complete defence the mere prove that the defendant was not aware that the company was insolvent at the time they entered into the transactions.

These above-mentioned defences are not available to (i) unreasonable director-related transactions; (ii) unfair loans; and (iii) circulating security interests. Thus, the transaction can be voided even if the defendant proves that he or she was not aware that the company was insolvent at the time he or she entered into the transactions.

QUESTION 2.1: 3/3

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?

The Model Law on Cross-Border Insolvency (MLCBI) provides in its article 20 (1) that:

"Upon recognition of a foreign proceeding that is a foreign main proceeding:
(a) Commencement or continuation of individual actions or individual proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;
(b) Execution against the debtor's assets is stayed; and
(c) The right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended."

However, the countries can adapt the Model Law to its own legal system and when Australia did it in 2008, it established that the stay under Article 20 of the Model Law as being the same as would apply if the stay or suspension arose under: "(a) the Bankruptcy Act; or (b) Chapter 5 (other than Parts 5.2 and 5.4A) of the Corporations

Act, as the case requires". So, the scope of the stay will depend on the case and the kind of proceeding that was opened abroad.

Thus, the court shall decide if the stay will affect both secured and unsecured creditors or only the unsecured creditors. In practice, the stay that has an impact on secured creditors (applied in the voluntary administration proceeding) is usually granted when the proceeding opened has the goal of restructuring the company from the financial distress (voluntary administration moratorium); the stay applied only to unsecured creditors commonly is given to proceedings that aim to pay creditors and close the company (liquidation moratorium).

QUESTION 2.2: 2/3

Question 2.3 [maximum 4 marks]

What are the differences between liquidations and small company liquidations?

The simplified liquidation process for small companies uses the rules of the ordinary liquidation regime with some adaptations to "make the process less complex, less costly and swifter, so as to ensure greater returns for creditors and employees".

This simplified liquidation process is available to companies which total liabilities do not exceed AUD 1 million and no current director of the company has been a director of another company that has used this simplified liquidation process. However, 25% or more in value of the creditors may refuse this simplified process.

The simplified liquidation process has some special rules comparing to the regular liquidation preceding:

- Voidable transactions: the return of assets applies only to unfair preferences of over AUD 30,000 paid to related parties of the company in the period up to three months before the beginning of the liquidation;

- It is only necessary to report potential misconduct to the ASIC when the liquidator has reasonable grounds to believe that misconduct has occurred;

- Creditor meeting is not compulsory as well as the committees of inspection;

- The proof of debt process is simplified; and

- special rules for electronic communications and voting.

QUESTION 2.3: 4/4

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

Commented [BB4]: Sub-total = 14 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.

Australia is considered a creditor-friendly system both generally and in its insolvency processes because the primary focus is on the protection of creditors’ rights in insolvency situations. There are several examples that confirm this statement, such as:

- The majority of Australian’s insolvency proceedings involve the appointment of an external administrator. This means that the large majority of the proceedings are not debtor-in-possession proceedings. In other words, the debtor’s managers are replaced by an external administrator. Only the schemes of arrangement and small business restructurings are debtor-in-possession proceedings, despite there is a qualified insolvency practitioner that must still be appointed as an advisor;

- As a general rule, secured creditors can enforce their claims during the bankruptcy and liquidation processes. Thus, the moratorium / stay order doesn’t prevent the secured creditors from enforcing their claims. In many countries, the stay order (moratorium) applies to all creditors, including the secured ones.

- appointment of a receiver: major creditors with security over the whole or substantially the whole of a company’s property are entitled to appoint a receiver over the top of a voluntary administrator;

- voidable transactions: Australia has broad law on insolvent trading liability for directors and a voidable transaction regime. Thus, it is easier to claw back sums and assets for the benefit of creditors.

On the other hand, the corporate voluntary administration regime and some recent reforms of Australian insolvency law are encouraging a stronger corporate and business rescue culture and promote a move away from the existing dominance of creditors’ rights. Among these reforms are:

- As of 1 July 2018, as a rule, creditors are prevented from enforcing ipso facto contractual rights contingent only on a company’s insolvency or entry into an external administration;

- As of 1 September 2017, the “safe harbour” allows companies directors to continue to allow a company to incur debts with a view to implementing an informal restructuring attempt, but under the supervision of a restructuring expert. If these conditions are met, the directors are free from insolvent trading liability;

- the voluntary administration regime aims to increase the chances of rescue of an insolvent company or restructuring its business as much as possible, under the terms of a DOCA.

Despite these recent modification on Australian law, the whole system is much more creditor-friendly. Generally speaking, the system is more focused in guaranteeing the creditors rights in order to keep the confidence in the financial system. To become more debtor-friendly, Australian system should create more options of debt-in-possession proceedings, like the one existing under the USA Bankruptcy Code (Chapter 11). Nowadays, debtor-in-possession proceeding exist only for companies with less than one million Australian dollars debt, under the new small company restructuring process and schemes of arrangement (which do not always involve insolvency).

Besides, to be more debtor-friendly, the moratorium (stay order) should be also applied to the secured creditors. This would give the insolvent company some breath space to reorganize its business.

14/15 marks - **this is a very good essay. It is to the point and accurately identifies the main aspects of Australia's insolvency regime which are creditor-friendly and those recent reforms which have tilted the scales slightly towards the debtors. It could only be strengthened by acknowledging the number of procedural rights which creditors have (eg the right to require IPs to provide information, the rights to vote out IPs with ease). Overall, very strong.**

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

Commented [BB5]: Sub-total = 13 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 Lyonesse 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 Lyonesse 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 Lyonesse liquidation.

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

*First of all, the ATO could question if Aussiebee's COMI (center of main interest) is really in Lyonesse or not. The definition of the COMI is paramount, since, if the Federal Court of Australia finds that the COMI of Aussiebee is in Lyonesse, the Lyonesse liquidation will be recognised as a foreign main proceeding under the *Cross-Border Insolvency Act 2008* (which enacted the *Model Law on Cross-Border Insolvency - MLCBI*). On the other hand, if ATO demonstrates that the COMI of Aussiebee is in Australia, not Lyonesse, ATO could ask for the Federal Court of Australia to not entrust the assets of Aussiebee to the Lyonesse liquidator.*

But what shall determine the place of the COMI?

*The leading Australian decision on COMI is the *Ackers v Saad Investments*. Basically, that decision followed the same principles adopted by the European Court of Justice in the *Eurofood Case (Re Eurofoods IFSC)*, which is the COMI is to be determined having regard to the objectively ascertainable factors of the debtor.*

There is a presumption that the COMI is located in the company's place of incorporation. However, there are some elements in this case that can set aside this presumption, like:

- The CFO is Australian and resident in Australia;*
- The vast majority of the directors are Australians;*
- The CEO is Australian;*
- The products are Australian and produced by its subsidiary in Australia.*

Nevertheless, even if the Federal Court of Australia finds that the COMI of Aussiebee is in Lyonesse (in the event that the COMI presumption prevails), the MLCBI provides in its articles 19 and 21 that the foreign representative may get a relief to be entrusted with the assets of the debtor located in the State where the recognition is sought. However, this kind of relief just can be given if the interest of local creditors is properly secured.

ATO could argue that ATO is not entitled to prove its credit in the Lyonesian liquidation, which means that the ATO wouldn't be paid under the Lyonesian proceeding. Thus, ATO can say that its interest as a local creditor is not properly secured. If all assets were to be delivered to the Lyonesian liquidation, ATO would not receive any dividend. This would be a violation of the pari passu principle.

In the Ackers v Deputy Commissioner of Taxation case, the Federal Court of Australia held that if a credit can't be proven in the foreign main proceeding, a relief that allows the foreign representative the realization of assets situated in the territory where the relief was granted is contrary to the pari passu principle and the security of local creditors. According to this precedent, ATO could enforce its claim in Australia in order to receive the same amount as it would receive if the proof of the debt was possible in the foreign main proceeding.

8/8 marks - very strong answer. Addressed the issues of COMI and stated the factors that may displace the presumption of COMI being the place of incorporation. Also addressed the issues regarding ATO receiving a pari passu distribution.

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?

The first thing to have in mind is that HA has continued to trade despite the fact its directors were already aware of its insolvency status since the judgment was handed down in October 2020. Although there is no legal obligation to a debtor to open a formal insolvency proceeding if it became insolvent, the continuation to trade in this condition may bring personal liabilities to its directors. If certain conditions are met that demonstrate that the transaction shouldn't had been made, directors can be subjected to insolvent trading and may have to pay damages to the company. It's important to highlight that the holding company HGL can also be liable for insolvent trading of HA. Generally speaking, the managers should take some actions to prevent the insolvency or, if it not possible, to reduce to loss of the company and its creditors.

Regarding the company's liabilities, the major debts are: (i) AUD 3 million borrowed from CBA. This an unregistered security but needs to be repaid in the short-term, (ii) AUD 5 million borrowed from HGL (its parent company) and (iii) AUD 30 million borrowed from a shareholder of HGL.

This last debt is an unsecured debt, but this contract has ipso fact right that provides that the loan becomes automatically due and payable in full if HA enters into any formal insolvency or restructuring process in Australia. It is important to point out the provision of section 451 E and 451 F (Corporations Act) which provides an ipso facto moratorium when the debtor starts a voluntary administration.

Concerning the debt with CBA, section 267 of the Personal Property Securities Act states that any unperfected security interest will automatically vest in the grantor (the

debtor, in this case) immediately prior to the commencement of a bankruptcy, voluntary administration or liquidation of the grantor. This also happens if the debtor goes into voluntary administration instead of liquidation.

Considering this situation, I would advise the Board to recognize the insolvency status of HA and would **initiate a voluntary administration**. If a voluntary administration is initiated there will be a stay on the claims from HGL shareholder and CBA. The stay is a breathing space to try a rearrangement with the creditors or at least a better liquidation of the company and, at the same time, try to avoid liabilities to the directors. After the voluntary administration, two outcomes are possible; **the company goes into a DOCA (and restructure its debts) or the company goes to liquidation. The DOCA could include the selling of the Perth re-refining plant in light of the offer of purchase the company has received.**

QUESTION 4.2: 5/7

* End of Assessment *