



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 = 28/50 (56%)

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

Commented [BB2]: Sub-total = 6 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

Commented [BB3]: The correct answer is (a)

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:

Commented [BB4]: The correct answer is (a)

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:

Commented [BB5]: The correct answer is (d)

Commented [BB6]: The correct answer is (d)

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: 6/10

QUESTION 2 (direct questions) [10 marks]

Commented [BB7]: Sub-total = 4 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:

1. Unfair preferences
2. Uncommercial transactions
3. Unreasonable director-related transactions
4. Unfair loans

5. Circulating security interests (in limited circumstances) p35

QUESTION 2.1: 2/3

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 Court should in a recognition application, consider what "the case requires". This entails whether the case requires the broader voluntary administration stay which in essence only affects secured creditors or if it requires a standard liquidation stay that would only affect unsecured creditors.

QUESTION 2.2: 1/3

Question 2.3 [maximum 4 marks]

What are the differences between liquidations and small company liquidations?

The differences are:

1. with a small company liquidation, the company's total liabilities do not exceed AUD 1 million.
2. The current directors of the company must not have been directors of other companies that have undergone restructuring or was subject to simplified liquidation process within seven years
3. A liquidator cannot adopt the simplified liquidation if at least 25% in value of the creditors voted in favour of the process

QUESTION 2.3: 1/4

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

Commented [BBB]: Sub-total = 9 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.

I agree with the statement.

Prior the recent reforms to the corporate insolvency regime, the law was overwhelmingly focussed on upholding creditors' rights and remedies, especially by actively assisting creditors to secure and enforce their claims and sequester and liquidate individuals and companies respectively.

The idea that creditors' rights should be balanced against, never mind being at times subsumed by, the rights and interests of debtors, their shareholders, management, and employees in an effort to encourage and assist indebted businesses to continue in business (or be rescued) was regarded as unworthy of consideration.

The law largely concerned itself with protecting creditors and their rights to the exclusion of other stakeholders. This skewed (even one-sided) emphasis had a negative impact on corporate revival and business rescue.

In a time of the dominance of creditors' rights, secured creditors were entitled to enforce their rights during a bankruptcy process and / or liquidation process while unsecured creditors relied on the Bankruptcy Act and Corporations Act to force individuals or companies to pay their debts. If not paid within a stipulated time, the creditors were entitled to forthwith apply to sequestrate (place in Bankruptcy) an individual or to liquidate of a company without regard to the negative consequences that may flow from such actions.

The notion that sequestered individuals would for several years be made to live under oppressive restrictions by being deprived of the rights and privileges enjoyed by their fellow citizens, such as to run their own bank account or apply for credit was not a consideration when deciding how an indebted individual should live his / her life post-becoming over-indebted.

Likewise, indebted corporate entities liable for liquidation were restricted in their ability to resist liquidation, or to remain in business or, if so allowed, only at the say-so of their creditors who would exercise their rights in such a way as to impose oppressive financial terms on the entity. The heavily pro-creditor legal regime led to many companies that would otherwise have been able to resume trade after compromising with their creditors or being given an opportunity to restructure, being placed in liquidation, and thus permanently depriving the entity of the opportunity to trade causing job losses, loss of shareholder capital, and removal of otherwise viable corporate entities from the Australian market.

As a result of the recent reforms, companies can now enter voluntary Administration (Part 5.3A of the Corporations Act), or a creditors' scheme of arrangement (under Part 5.1 of the Corporations Act) or for companies with a liability of less than AUD 1 million a restructuring process and plan under the new Part 5.3B of the Corporations Act (which came into effect on 1 January 2021). A company now has an opportunity to restructure and so to speak lift itself out of debt and continue their existence.

Creditors can no longer enforce contractual rights, apart from certain exclusions, thereby giving the company a better chance of survival. Directors of a company can now proceed to trade without the fear of personal liability, a "safe harbour", under the professional supervision of an appointed professional. By doing this the arrangement will provide a better return for the company's creditors. Employees will retain employment and suppliers can continue trading with the company.

In the matter between *Mighty River International Ltd v Hughes (2018) 265 CLR 480*, a decision of the High Court of Australia emphasised that a DOCA can hold off distribution of property to creditors thereby placing a suspension on claims from creditors with the understanding that an assessment by the appointed administrator must indicate that it would be a better outcome for creditors to proceed with the voluntary administration rather than liquidation of the company.

9/15 marks – the essay speaks in very high-level terms about Australia's insolvency regime and fails to interact with its more substantive aspects. The essay identified the small

business restructuring process and the safe harbour provisions for insolvent trading. It failed to identify the ipso facto moratorium which works in favour of debtors' rights. It does not address the mass of procedural rights which creditors have (eg right to require IPs to provide information, easier to vote out IPs etc). It acknowledges that, traditionally, Australia's insolvency regime was creditor-friendly but does not note that the recent reforms have worked in the other direction to better uphold the rights of debtors/bankrupt individuals/insolvent companies.

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

Commented [BB9]: Sub-total = 9 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?

Answer

In summary, the question is whether, given the facts, can ATO claim pari passu payment of Aussiebee's tax liability given the provisions of Australia's Cross-Border Insolvency Act of which the Model Law is part. Put differently, can ATO take steps to prevent the Lyonesse appointed liquidator of Aussiebee from obtaining an order realizing and removing all

Aussiebee's assets from Australia to Lyonesse for general distribution to the general body of creditors in the Lyonesse run liquidation (to the exclusion of ATO).

The liquidator has quite properly brought an application in terms of the Cross-Border Insolvency Act, 2008 (of which the Model Law is part) to have the Lyonesse liquidation recognised as a foreign proceeding. It is her request for an order that the assets be removed to Lyonesse which is contentious.

While in principle such orders are commonplace, the issue in this instance is whether domestic creditors, particularly those incapable of proving their claim in Lyonesse, can enforce their domestic creditor rights in Australia, especially given that the debt in this instance is a tax debt not recognised by, nor claimable, in Lyonesse. Put differently, as ATO is not recognised as a creditor in Lyonesse for the debt, it will not be recognised as a member of the general body of creditors in Lyonesse and thus not share in the proceeds of liquidation.

In 2008 Australia adopted the UNCITRAL Model Law on Cross-Border Insolvency as a Schedule to the Cross-Border Insolvency Act 2008, thus giving the Model Law the force of law in Australia albeit with modifications. In Akers v Deputy Commissioner of Taxation, the lower court had to decide on the application of the Model Law in circumstances where a foreign liquidator wishes to remove assets from Australia for distribution to the general body of creditors in circumstances which would deprive the DCT from having its domestic claim to those assets for settlement of a tax liability satisfied. The court held that the Model Law could not be interpreted to deprive the DCT from attaching sufficient assets in Australia to satisfy its domestic claim *pari passu*. Important considerations favouring this interpretation was the fact that the Model Law should not be interpreted as prejudicing or lessening existing domestic rights, tax liability claimable by the DCT constituted a legitimate domestic (Australian) debt albeit a claim which would not be recognised under Lyonesse law and thus the DCT would not be able to participate in and benefit from the distribution of the realized assets in Lyonesse. Also, that the Model Law should not be interpreted in such a way as to not recognise domestic claims, especially those that would be unclaimable in the foreign jurisdiction. As a tax liability, and the public interest consideration flowing from that, especially the loss of tax revenue should the assets be transferred in toto to Lyonesse, the Full Federal Court on appeal upheld the lower court's order that:

1. When granting or modifying relief under the Model Law, the Court must ensure that the interest of local creditors are protected, and
2. The primary judge, by permitted the DCT to recover only a *pari passu* entitlement to the assets, acted correctly by upholding the principles of fairness between all creditors.

Based on the **Aker** judgment, the ATO is accordingly advised to apply to intervene in the recognition and removal proceedings in Australia, to seek an order that the ATO be permitted to recover its *pari passu* entitlement to the assets before the assets are released to the liquidator and removed to Lyonesse. Accordingly, Aussiebee's assets in Australia may be sent to Lyonesse only after the ATO's *pari passu* share had been recovered and, in this way, the domestic debt owed to ATO will be properly recognised and paid (albeit *pari passu*).

4/8 marks – this answer only addressed half of the issues which should have been addressed. It is true that, applying *Ackers*, the the ATO should enforce its claim in Australia for the purpose of recovering an amount up to the *pari passu* amount it would have received as an unsecured creditor in the Lyonesse proceeding. However, the answer failed to deal with the preliminary issue of AussieBee's COMI. The answer did not address COMI at all. Marks were dedicated to identifying that the ATO could intervene on the basis that there was sufficient facts to displace the presumption that AussieBee's COMI was in its place of incorporation.

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

I would advise the boards that as HA is incorporated in Australia under the Corporations Act, HA's board of directors ought to resolve to place **HA under Voluntary Administration ("VA") (to be followed up by a DOCA - deed of company arrangement)** under section 5.3A of the Corporations Act as HA appears to be trading, or is at least on the brink of trading in insolvent circumstances given the level of indebtedness and the fact that the time to begin repaying substantial loans is imminent.

As to the existing debtors, the following:

1. A shareholder of HGL lent USD 30 million (unsecured) to HA and currently has little to no prospect of being repaid by HA from income generated from its trading operations with effect from end 2021. Moreover, HA and the shareholder entered into an agreement that the full loan will become payable if HA enters any formal insolvency or restructuring process ("the acceleration clause"). As a VA is not considered to be a "formal insolvency or restructuring process", a VA will not trigger the acceleration clause. HA will thus avert the prospect of the shareholder instituting formal liquidation proceedings against HA (should be unable to repay the debt which it surely cannot), and the VA will provide HA with a moratorium against payment of the onerous month payments due to the shareholder from due date until the VA has run its course, or the DOCA is approved, and therefore relieve the current pressure on HA's cashflow.
2. Via VA, HA can avert an action brought by CBA for repayment of AUD 3 million based on the mortgages passed over the trucks. Because CBA omitted to register the mortgages on the Personal Property Securities Register, CBA is precluded from enforcing its rights by means of an action in an appropriate court having jurisdiction. Failure to have registered the mortgage bonds at least six months before the VA means that CBA cannot take priority as a secured creditor in liquidation. In fact, failure to register results in the unperfected security interest automatically vesting in HA as the grantor (save for the possibility that a court may grant CBA an extension of time within which to register the mortgages). This scenario presents HA with an opportunity to persuade CBA to co-operate in the VA knowing that the prospect of being repaid in a liquidation is greatly diminished as it will, in that case, be compelled to share in the distribution as an unsecured creditor together with all other unsecured creditors.
3. HGL, having lent a sum of USD 5 million to HA, is likely to support the VA as its loan is unsecured and HGL is unlikely to recover the monies lent if HA is placed in liquidation given the size of the claims that will be proven should HA be liquidated.
4. BOR has a judgment against HA in the sum of AUD 4.6 million which, if BOR chooses to make demand, HA will be unable to satisfy thus entitling BOR to apply for HA's liquidation. This possibility can be averted by commencing a VA.
5. The board is advised that the directors have fiduciary duties towards HA and HGL and third parties. If HA is liquidated (and HGL may also face liquidation should HA be

unable to repay the USD 5 million it lent to HA), the liquidator is entitled to pursue steps against the directors should he establish that the directors knowingly allowed HA or HGL to trade under insolvent circumstances. The directors will then face damages claims in their personal capacities. This is a remote possibility however as HA appeared to have traded in good faith and even made a profit albeit small.

A VA is often used as a vehicle to achieve a business rescue via a sale of the business as a going concern to a third party. Given the level of indebtedness and the interest shown by a third party in purchasing the Perth plant, the board is advised to strongly consider proceeding to VA without delay. While preparing a subsequent DOCA, the existing creditors can be approached to re-arrange and / or compromise their claims against HA. It is likely that creditors will be willing to do so as otherwise they face the prospect of not recovering a substantial portion of the debt owed to them in liquidation proceedings.

Question 4.2: 5/7

*** End of Assessment ***