

LAWS50093 Insolvency Law (2018 SEM 2)

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Stakeholders

- Debtor: [●]
- Director of debtor: [○]
 - Not to breach director's duty
 - Not to be responsible for insolvent trading
 - Be confident about [●]'s financial situation
 - Independent director ⇒ Not responsible to the shareholders
 - Executive director
- Creditor: [■]
 - Secure director's guarantee
 - [●] stays in business as a going concern
 - Priority creditor
 - Secured creditor [□]
 - Shareholder of [●]
 - Unwilling creditor: eg, employee (wages, superannuation, long service leave)
- Customer
- Supplier
- Insolvency practitioner: [▲]
- Public
 - Keep the major employer in sound business
 - Tax Commissioner

[...] is the holding company of [●] because

- [...] is in a position to cast / to control the casting of more than more than 50% votes that might be cast at [●]'s general meeting (CA s 46(a)(ii)).
- [...] holds more than 50% of [●]'s issued share capital (CA s 46(a)(iii)).
- [...] controls the composition of [●]'s board (CA s 46(a)(i)) because [...] can, by exercising legally enforceable power, appoint / remove all majority of [●]'s directors. [...] has such power because according to ...,
 - ... [●]'s constitution,
 - ... agreement between [●] and [...],
 - ... statutory requirement under ...,... [○] cannot be appointed as [●]'s director without ...
 - ... [...] exercising power in [○]'s favour (CA s 47(a)).
 - ... [○] being a director of [...] (CA s 47(b)).

- [...] and [●]
- [●] and other subsidiaries of [...]

... are therefore related companies (CA s 50(a)(b) / s 50(c)).

Commencing Bankruptcy

I. Involuntary Bankruptcy

- [●] commits an act of bankruptcy in failing to ...
- ... comply with a bankruptcy notice (*BA* s 40(1)(g)) which has been properly served to [●] (can be left at [●]'s last known address (*Bankruptcy Regulation 2006* (Cth) regs 16.01, 16.02)),
 - ... satisfy execution issued against him under process of a court (*BA* s 40(1)(d)(ii)),
- ... which in turn creates a rebuttable presumption that he is insolvent (*BA* s 52(2)).

To avoid the serious and quasi-penal nature of a sequestration order (*Wolff v Donovan*), [●] might want to challenge the final judgment(s) (totalling ... (must be at least \$5K (*BA* s 41(1))) based on which [■] obtained the bankruptcy notice against [●].

- To invalidate the notice because the amount specified in the bankruptcy notice exceeds the amount in fact due, [●] must, within the time allowed for payment, give notice to [■] that he disputes the validity of the notice on the ground of misstatement (*BA* s 41(5)).
- [●] might want to invoke the inherent jurisdiction of the FCA / FCCA (*BA* s 41(7)) to set aside the bankruptcy notice because ...
 - ... the notice contains fundamental defect or error because it does not clearly state that the debt is owing and how much the debt is (cf *Kleinwort Benson v Crawl*).
 - Instead of requiring payment in accordance with the judgment, the notice requires payment of the overdue instalments, an arrangement not qualifying as final judgment or order (*Kleinwort Benson v Crawl* at 78-79 (discussing *In re HB*)).
 - Although interest due on a judgment debt need not be included in a bankruptcy notice (*Adams v Lambert* [19]), the interest that is included must be calculated (*Kleinwort Benson v Crawl* at 78).
 - Since textual and contextual reading of *BA* s ... reveals that the requirement of ... is made essential by the *Act*, a failure to comply with the requirement is not a formal defect or irregularity within the meaning of s 306 (*Adams v Lambert* [28]).
 - ... the defect or irregularity, though formal (*BA* s 306), has caused substantial injustice which cannot be remedied by an order of the court (*BA* s 306(1)).
 - The overstatement / expression of ... is objectively capable of misleading [●] as to what is necessary to comply with the notice (*Kleinwort Benson v Crawl* at 79-80 / *Adams v Lambert* [27]).
 - ⇔ Although the notice misstated the legal basis upon which the interest is calculated, the amount of interest is correctly calculated and stated (*Adams v Lambert* [19]).
 - ⇔ The irregularity in appointing trustee does not affect the act done by the trustee in good faith (*BA* s 306(2)).

Recovery Proceeding in Winding Up

[▲] may avoid the ... entered into / given effect to

... unfair preference (s 588FA) constituting insolvent transaction (s 588FC) ...	... in the period of six months before the relation-back day and the commencement of the winding up proceeding (s 588FE(2)(b)(ii)).
... <u>uncommercial</u> transaction (s 588FB) constituting insolvent transaction (s 588FC) ...	... in the period of two years before the relation back day (s 588FE(3)(b)) and the commencement of the winding up proceeding (s 588FE(2)(b)(ii)).
... insolvent transaction (s 588FC) with a <u>related party</u> ...	... in the period of four years before the relation back day (s 588FE(4)(c)) and the commencement of the winding up proceeding (s 588FE(2)(b)(ii)).
... insolvent transaction (s 588FC) for the purpose of / including defeating creditor's rights in the winding up ...	... in the period of ten years before the relation-back day (s 588FE(5)(c)) and the commencement of the winding up proceeding (s 588FE(2)(b)(ii)).
... unfair loans (s 588FD) ...	... on or before the commencement of the winding up proceeding (s 588FE(6)).
... unreasonable director-related transaction (s 588FDA) ...	... in the period of four years before the relation-back day and the commencement of the winding up proceeding (s 588FE(6A)).
... transaction with the intention to avoid employee entitlements (ss 596AB(1), 596AC(2)).	
... circulating security interest (s 588FJ) ...	... in the period of six months before the relation back date and the commencement of the winding up proceeding (s 588FJ(1)).
... security interest in favour of (an associate of) [●]'s officer because such person takes steps to enforce the security interest within the six months after the instrument creating the security interest is made (s 588FP(1)).	
[insolvent trading]	

I. Preliminary

The conveyance / transfer / giving of security / giving of guarantee / payment / incurrence of obligation / release by [●] / loan constitutes transaction within the meaning of Pt 5.7B (s 9).

Since [●] went into liquidation ..., the relation-back day is

... without undergoing administration or prior liquidation, ...	... when the application was filed (s 91, item 14; s 513A).
... upon court's order in administration after the application for winding up was filed, ...	... when the application for winding up was filed (s 91, item 2).
... voluntarily without prior liquidation or administration, ...	... when members passed the resolution to wind up [●] (s 91, item 15; s 513B).
... after executing a DOCA, ...	... when the administration began (s 91, item e; s 513C).

Case Notes

Adams v Lambert (2006, HCA)	Bankruptcy notice (set aside, <i>BA</i> s 306)
<p>Whether a bankruptcy notice should be set aside because a misstatement of the statutory provision under which interest on the judgement debt was claimed.</p> <p>[17] A bankruptcy notice is a proceeding under <i>BA</i>.</p> <p>[19] The calculation of post-judgment interest is a well-known source of difficulty for some drafters of bankruptcy notices. The difficulty is sometimes avoided by refraining from including interest in the debt upon which the bankruptcy notice is based.</p> <p>[21] The bankruptcy notice, as a written instrument, must be construed as a whole: words may generally be supplied, omitted or corrected, in an instrument, where it is clearly necessary in order to avoid absurdity or inconsistency.</p> <p>[26] The question of construction raised by the words ‘a formal defect or an irregularity’ is one to be decided by reading s 306 in the context of the whole <i>BA</i>, informed by the general purpose of the legislation, and the particular purpose of the provisions relating to bankruptcy notice.</p> <p>[27] What this Court regarded as relevant to s 306 was misleading a debtor about what is necessary to comply with the notice.</p> <ul style="list-style-type: none"> • [28] If a requirement is made essential by the <i>BA</i>, then a failure to meet that requirement is not a formal defect or an irregularity within the meaning of s 306. <p>The irregularity does not invalidate the bankruptcy notice:</p> <ul style="list-style-type: none"> • [19] The calculation of interest was correct. • [19] The bankruptcy notice made it plain, in express terms, that the interest claimed was post-judgment interest. 	
Air Services Australia v Ferrier (1996, HCA; Dawson, Gaudron and McHugh JJ)	Preference (running account defence)
<p>The liquidators sought to recover all the payments for air navigation, meteorological, fire-fighting, safety and other services provided to Compass as a condition of it being permitted to fly and land aeroplanes at Australian airports, all of which made in the preference period. Air Services Australia relied on a running account defence, saying that the entirety of the payments made during the six months period should be effectively treated as one payment and the liquidators were only entitled to recover the net amount by which Compass Airlines’ indebtedness had been reduced over that period.</p> <p>501: For the purpose of s 122, the effect of a payment on the other creditors of the debtor is determined objectively. If the payment has the effect of giving a creditor a preference over the other creditors, it does not matter that neither the creditor nor the debtor intended to give the creditor preferential treatment.</p> <p>502: If the purpose of the payment is to induce the creditor to provide further goods or services as well as to discharge an existing indebtedness, the payment will not be a preference unless the payment exceeds the value of the goods or services acquired.</p> <ul style="list-style-type: none"> • 502: A payment made during the six months period cannot be viewed in isolation from the general course of dealing between the creditor and the debtor before, during and after that period. Resort must be had to the business purpose and context of the 	

<p>payment to determine whether it gives the creditor a preference over other creditors.</p> <ul style="list-style-type: none"> • 502: To have the effect of giving the creditor a preference, priority or advantage over other creditors, the payment must ultimately result in a decrease in the net value of the assets that are available to meet the competing demands of the other creditors. 	
<p>Aussie Vic Plant Hire v Esanda Finance (2008, HCA; Gleeson CJ, Kirby, Hayne, Crennan and Kiefel JJ)</p>	<p>Offsetting claim</p>
<p>AVPH applied to have a statutory demand set aside. A master of the VSC declined to do so, but granted an extension of time for compliance. While appealing during the extended period to a single judge, AVPH failed to satisfy the demand. The extension duly expired. AVPH then applied for a further extension, pending the appeal. The appeal and application for extension of time were heard simultaneously. Both were dismissed, the judge concluding that the consequences foreseen by s 459F(1), had already come into play. AVPH unsuccessfully appealed to the VCA and further appealed to the HCA. The issue in the appeal was whether the time for compliance with a statutory demand could be extended after such time had expired.</p>	
<p>One of the main purposes behind Pt 5.4, is the speedy resolution of applications for winding up in insolvency. It would be sharply at odds with such a purpose to read the power to extend time for compliance with a statutory demand as capable of exercise after the time has expired. The point is put beyond doubt when regard is had to the consequence that the <i>Corporations Act</i> attaches to a failure to comply with a statutory demand. If a company fails to comply with a statutory demand, and that failure occurs during or after the three months ending on the day when that winding-up application is made, the court must presume that the company is insolvent. It is s 459C that requires the court to make that presumption. AVPH's argument could find no textual footing in s 459F(2). Although s 459F(2)(a)(i) refers to 'the last such order' extending the time for compliance with a statutory demand, that cannot include an order made after the period has expired. To read 'the last such order' as including an order made after the period for compliance has expired, would focus attention upon the state of affairs at either the date of commencement of the winding-up application or the date of the hearing of that application. However, s 459C neither requires nor permits that focus. It directs attention to what has happened at any time during a period, not upon a state of affairs at either the commencement or hearing of the winding-up application. Further, it is of fundamental importance to recognise that the provisions in question do no more than create a presumption about the ultimate issue that arises in an application to wind up in insolvency: is the company insolvent? Denying the power of a court to extend time for compliance with a statutory demand after the time has already expired determines no right or liability of the company or of the party that has made the demand.</p>	
<p>Clyne v DCT (1984, HCA; Gibbs CJ, Murphy, Brennan and Dawson JJ)</p>	<p>Voluntary bankruptcy</p>
<p>After a creditor's sequestration petition had been filed in the FCA, and before it was heard, Clyne filed a petition for sequestration of his estate, and the Registrar accepted it. <i>BA</i> s 55(3)(b) provides that on acceptance of a debtor's petition by the Registrar, 'by force of this</p>	