

INSOLVENCY 20 MARCH 2014 EXAM

EXAMINER'S COMMENTS

QUESTION 1

This question required students to identify that non-compliance with a statutory demand would result in a presumed act of insolvency under the Corporations Act, which could lead to a successful application to wind up the company. The appropriate advice to the company would be to either pay the money due under the demand, or make an application to set aside the statutory demand. The possible grounds would have been:

- (a) A genuine dispute about the extent of the debt – the services were “sub-standard” which may mean that not all of the contracted services were provided, leading to not all of the price under the contract being payable;
- (b) An offsetting claim – for the expenses involved in fixing problems with the work done, and damages suffered by customers leaving the company and going elsewhere;
- (c) The defect in the demand – there is nothing in the facts to suggest that the demand was defective, but one would need to see the demand to give advice;

- (d) Some other reason – in this case the serving of a statutory demand could be an abuse of process since there was a compulsory mediation clause in the contract.

Students had to identify the relevant sections and explain the criteria under each section for setting aside the demand. Students were also expected to identify the documents which should be filed to apply to set aside the statutory demand, including originating process and necessary affidavits in support. Students were also expected to identify the time limit for taking action.

QUESTION 2

This question was about voidable dispositions under the Corporations Act.

- (a) This could have been an unreasonable director-related transaction. Students were expected to identify the statutory criteria for such a voidable disposition, and consider the evidence which should have been sought to ascertain prospects of successfully challenging the bonuses;
- (b) This could have been an uncommercial transaction (i.e. an undervalue) or a transaction designed to defeat creditors. The necessary statutory criteria for each kind of voidable transaction should have been identified. The question of whether this was an uncommercial transaction would have depended upon the state of the book debts in 2010, as well as the state of the company.
- (c) This could have been an unfair preference. Students were expected to identify the statutory criteria for an unfair preference. The proximity to the

company going into liquidation would have been important in deciding whether it was an insolvent transaction.

- (d) This could have been an unfair loan, but the fact that it was obtained 13 years ago when the company was first incorporated could mean that the interest rate was not unfair. It was of relevance that the company had managed to pay the interest on the loan ever since.

For each kind of voidable transaction, as well as identifying the statutory criteria, students were expected to say whether or not the liquidator had to show that it was an insolvent transaction, and also advise the time limits which were applicable. Better answers referred to the test for insolvency (both statutory and case law), as well as referring to rebuttable presumptions of insolvency.

QUESTION 3

This question required students to recognize that Dave had already committed an act of bankruptcy by ignoring the Bankruptcy Notice. It was incorrect to suggest that an application could now be made to set aside the Bankruptcy Notice, as such an application can only be made before the time for compliance has expired. There is no possibility of extension of time. This being the case, the action which Dave could take would be to appear and oppose the Creditor's Petition. It is incorrect to suggest that he had to make an application to "set aside" the Petition.

However, on the hearing of the Creditor's Petition, Dave could argue that the Bankruptcy Notice was defective, and thus there was no valid act of bankruptcy on

which to found the Petition. This argument could have arisen because of the obvious overstatement of the amount due under the Bankruptcy Notice. It was an error to suggest that Section 41(5) could be used to give a notice about overstatement of amount, as this too is a remedy only available before time expires. Reference should then have been made to the prescribed cases dealing with errors in Bankruptcy Notices.

The other possible grounds of opposition would have been to challenge whether the Bankruptcy Notice was validly served (and in this regard it must be noted that the Regulation regarding service is not mandatory but only facilitative). Another possible ground of opposition would have been the solvency of Dave. It was not a viable ground of challenge to suggest that the default judgment could have been set aside and the court asked to go behind the judgment. Clearly Dave owed all of the money.

Full answers dealt with the documents which should be filed to allow Dave to appear at the Hearing and oppose the Petition.

QUESTION 4

This question was directed towards advising the date of the commencement of the bankruptcy (i.e. the relation-back period) and analysing whether the various assets were available to the trustee under relation-back, or whether any of the property was exempted. The question specifically said that the void disposition provisions were not to be considered.

The date of the commencement of bankruptcy was 27 August 2012 i.e. 21 days after service of the Bankruptcy Notice on 6 August 2012. The date of commencement was not the date of the District Court judgment, or the date of issue of the Bankruptcy Notice or date of service of the Bankruptcy Notice. As to the assets:

- (a) This painting was given away prior to commencement of the relation-back period. The trustee was not interested in pursuing a void disposition claim, and thus could not claim the painting.
- (b) The racehorse was sold after the commencement of the bankruptcy, but a defence would probably have been available under Section 123.
- (c) Personal means of transport may be exempt, but only if the vehicle has a modest value. The prospect also existed that this was a leased motor vehicle, in which case it was not available to the trustee.
- (d) Money in a self-managed superannuation fund is not available to the trustee as it is exempt, but this is subject to Section 128B, which enables the trustee to obtain funds paid to a superannuation fund if the purpose has been to avoid creditors.
- (e) If the loan was a secured loan, then the bank was entitled to repayment. If the loan was unsecured, then the trustee could claim the funds paid to the bank. However, the bank could well have a defence under Section 124.

QUESTION 5

This question concerned void dispositions under the Bankruptcy Act. They were:

- (a) A transfer for less than full consideration which could be attacked under Section 120. A possible defence was available to the wife if the transfer occurred at a time when Frank was solvent. Students were expected to identify the time limit for this defence and to discuss the statutory and case law requirements for proof of solvency.
- (b) These payments could have been challenged under Section 128B, and students were expected to identify the test of purpose. Students should have identified the factors to be taken into account in deciding purpose, particularly the pattern of payments. The pattern included not only the dates of payments, but the amounts. The rebuttable presumption available to the trustee should have been discussed.
- (c) This gift was so long ago that the only section which could have been used to challenge it was Section 121. Students were expected to identify the purpose which had to be proved by the trustee, and discuss the available presumptions. Not only can void dispositions be challenged, but the proceeds of a void disposition can be traced into other property. The defence under Section 121 should have been discussed.