

## Episode 26: Summary

**Episode name:** Complex Bankruptcies

**Guest(s):** Mark Robinson

**What area(s) of law does this episode consider?**

Primarily bankruptcy. This episode also touches on the impact of holding assets in discretionary trusts and superannuation funds, in addition to the impact of family court proceedings and voidable transactions. It also considers cross-border insolvency law.

**Why is this topic relevant?**

In this episode, experienced liquidator Mark Robinson, explores the intricacies of complex bankruptcies through a storytelling dialogue of some high-profile cases he has been professionally involved in.

**What legislation is considered in this episode?**

*Cross-Border Insolvency Act 2008 (Cth)*

*Model Law on Cross-Border Insolvency of the United Nations Commission on International Trade Law (UNCITRAL)*

*Bankruptcy Act 1996 (Cth)*

- Section 58: Upon a person becoming bankrupt all property belonging to the bankrupt is divisible amongst creditors. Except property held on trust for another person as per section 116(2)(a).
- Section 81: A trustee, receiver or creditor who has a debt provable in the bankruptcy can apply to the court for an examination of an associated entity in relation to the bankruptcy.
- Section 121: Transfers will be deemed voidable where they are done in an attempt to prevent, hinder or delay creditors from getting a share of the property.
- Section 73: A bankrupt can make a proposal to creditors, which has to be approved by special resolution, to resolve the debt.
- *Bankruptcy Amendment (Enterprise Incentives) Bill 2017 (Cth)*

**What complex bankruptcy and common law cases are considered in this episode?**

**Ray Williams**

- In 1968, Ray Williams co-founded HIH Insurance Limited which was Australia's second largest general insurer.
- During his appointment as CEO from 1998-2000, executive bonuses multiplied x20 and he purchased FAI Insurance without conducting due diligence. At the time, Williams' personal wealth was \$14 million (mostly HIH shares).
- After his resignation as CEO in 2001, McGrath Nicol revealed HIH Insurance losses of \$5.3 billion during Williams' appointment – the largest corporate collapse

in Australia to that date.

- In May 2002, Williams was ordered to pay \$8 million worth of compensation after ASIC successfully sued for breach of directors' duties.
- In 2005, a Royal Commission was held to investigate the collapse of HIH and Williams was sentenced to jail for 4.5 years for lying in company prospectuses.
- Ray Williams declared bankruptcy when HIH's liquidator sought return from Williams of \$1 million as part of his termination payment when he exited as CEO in 2000.

### **Geoffrey Edelsten**

- Edelsten was a wealthy doctor in NSW who established luxury medical clinics during the 1980s.
- In 1990 he was sentenced to jail for soliciting Christopher Dale Flannery to assault a former patient planning to sue Mr Edelsten for poor procedure.
- In 2005, Edelsten founded Allied Medical Group which was sold to Sonic Group in 2011 for over \$100 million.
- Edelsten relocated to the US and went into business with Mr and Mrs Mawardi who owned a boutique store, House of Nurielle, in Las Vegas.
- In 2011, post-GFC, Edelsten instructed Mawardi to purchase distressed property for him to invest in.
- By 2012, Edelsten and Mawardi had fallen out and filed court proceedings against each other. Edelsten was found to be owing over \$14 million to the ATO.
- Edelsten filed for bankruptcy in the USA in January 2014. Sonett Kapila in Florida was appointed trustee who made an application for recognition in the Federal Court of Australia where Justice Beach recognised the bankruptcy ordered restraints on Mr Edelsten's Australian-based assets and appointed Mark Robinson as Sonett Kapila's agent in Australia.

### **John Cummins QC**

- Cummins became a solicitor in 1957 and was part of the Queen's counsel in 1980.
- In August 1987, 13 years prior to his eventual bankruptcy, he disposed of all his assets by transferring them to his wife or his family trust.
- In the late 1990s, journalist Paul Barry broke the story in the Sydney Herald about barristers facing unpaid tax bills who claimed bankruptcy, including Cummins.
- In 1999 the ATO discovered Cummins was not lodging tax returns, and it wasn't until 2000, 45 years after being admitted as a solicitor, that Cummins paid his first tax return which was for the years 1992-99.

- According to his income assessment, the ATO claimed \$1 million was payable in tax, after which Cummins declared bankruptcy.

**Lewis v Condon [2013] NSWCA 204:** In this case the NSW Court of Appeal held that a trust was not a sham despite being created with the intent to deceive others. The Court said, "although the [relevant] trust was created with an intent to deceive others, the primary judge was right to conclude that it was not a sham trust". In the Court's view, in order for there to be a sham, it was necessary there be an intention that the discretionary trust created not bear its apparent legal consequence. While there was an improper purpose, the Court said, "this was entirely consistent with the creation of a genuine discretionary trust". Of paramount importance is whether there was any intention to create a trust.

### What are the main points?

- Bankruptcy law today more closely parallels the law of corporate insolvency. The fundamental principle is *pari passu* which literally means 'on equal footing' – meaning that all unsecured creditors must share equally, in any monetary distribution, in proportion to the debts due to each creditor.
- Three main factors indicate a complex bankruptcy: 1) personality of the bankrupt; 2) structure and conduct of a bankrupt's affairs pre-bankruptcy; and 3) where a bankrupt has access to significant funds through friends and family.
- A complex bankruptcy typically involves previous heads of industries who at one point had control over millions if not billions of dollars.
- Pre-planning of a complex bankruptcy will involve research on media articles and court reports concerning the bankrupt.
- A creditor's petition is a document filed in the Federal Circuit Court where a creditor requests a sequestration order.
- The Australian Financial Security Authority (also known as AFSA) manages the application of bankruptcy and personal property securities laws in Australia.

### What are the practical takeaways?

- Family law courts are able to hear bankruptcy matters too, as they are both governed by federal legislation. Often the involvement of family court orders can increase complexity of the bankruptcy.
- Pre-planning in a bankruptcy can assist in gaining beneficial outcomes for creditors in a bankruptcy, particularly in both identifying and locating assets. It is also beneficial to identify the location of the proposed bankrupt so that service can be effected.
- Bankruptcy investigations can be costly, particularly if assets have been hidden or transferred to a third party. However, there is little point in pursuing investigations unless you have sufficient funds to reach a conclusion. Funding is usually provided via realisation of available assets or creditors.

- A Personal Insolvency Agreement (or a Part X Agreement) allows a debtor to make an agreement with their creditors without going through the bankruptcy process, which will be less costly and give greater returns to the creditors.
- In recent years there has been a push for a one-year bankruptcy scheme, however, this is perhaps an undesirable scheme in relation to high-profile complex bankruptcies where the trustee needs appropriate time and resources to conduct their investigations and realise and distribute assets.
- Under section 73, a bankrupt can make a proposal to creditors, which has to be approved by special resolution, to resolve the debt – this operates as an annulment.
- Communication between a bankruptcy and creditors is key to achieving the best possible outcome for creditors.
- Public examinations are a useful tool for trustees to obtain information about the bankrupt from their friends, lawyers, family and other associated entities.
- In response to the COVID-19 pandemic, the Australian government has increased the amount needed to be owed by a creditor to file a creditor's petition from \$5,000 to \$20,000, to provide temporary relief to financially distressed individuals.

#### Show notes

[James McGrath's second reading speech on the Bankruptcy Amendment \(Enterprise Incentives\) Bill 2017](#)

[Mark Robinson's article 'Large and complex bankruptcy - Maximising returns for creditors'](#)