

**Baker
McKenzie.**



**THE "IPSO FACTO" PROHIBITION IN
THE CORPORATIONS ACT APPLICABLE
TO CORPORATE INSOLVENCY**



IpsO facto clauses

An ipso facto clause is a contractual provision that allows one party to the contract to terminate or modify the operation of the contract upon the occurrence of a specified insolvency related event (such as the appointment of an administrator, receiver or liquidator) in respect of another party.

Examples include:

- a clause that entitles a landlord to terminate a lease in the event that an administrator is appointed to the tenant; and
- a right to terminate arising under a loan agreement caused by the borrower making a court application in relation to a proposed creditors' scheme of arrangement.

Stay on enforcement of ipso facto rights

From 1 July 2018, a moratorium on reliance on "ipso facto" contractual clauses triggered by the counterparty becoming subject to certain specified formal corporate insolvency events came into effect.¹

In summary, the ipso facto moratorium (or stay) means that there will be a stay on the enforcement of certain ipso facto contractual rights against companies the subject of any of the following insolvency regimes:

- a creditors' scheme of arrangement (including certain steps leading up to the scheme);
- a voluntary administration; or
- a receivership but only where the receiver is appointed over the whole or substantially the whole of the property of the company,

if those rights have become enforceable because of the fact of the counterparty becoming subject to that insolvency regime. It also extends to a right triggered by the counterparty's financial position if it is subject to one of the above insolvency regimes. The stay also applies to "self-executing" provisions which are triggered by such events.

However, the stay does not apply by reason of the counterparty becoming subject to the following insolvency regimes:

- a receiver or other controller appointment that is not over the whole or substantially the whole of the company's property;
- a deed of company arrangement;
- a liquidation (at least in circumstances where the liquidation does not immediately follow an administration or creditors' scheme).

Where the operation of an ipso facto clause is stayed, the ability of the counterparty subject to the insolvency regime and having the benefit of the stay to enforce a right under a contract for new advances of money or credit is also stayed.

It is important to note that the stay is not intended to restrict a counterparty from enforcing a right (or to disapply self-executing provisions) for any other reason, such as a breach involving non-payment or non-performance.

Application of the stay

Subject to the exceptions set out below, the stay applies to all contracts, agreements or arrangements entered into on and from 1 July 2018.

Note that the stay does not apply to variations or novations to contracts where the original contract was entered into prior to 1 July 2018, but only where such variation or novation is made before 1 July 2023.

¹ The relevant provisions are contained in section 415D of the *Corporations Act 2001 (Cth)* (Act) in respect of creditors' schemes of arrangement, section 434J of the Act in respect of receivership and section 451E of the Act in respect of voluntary administration.

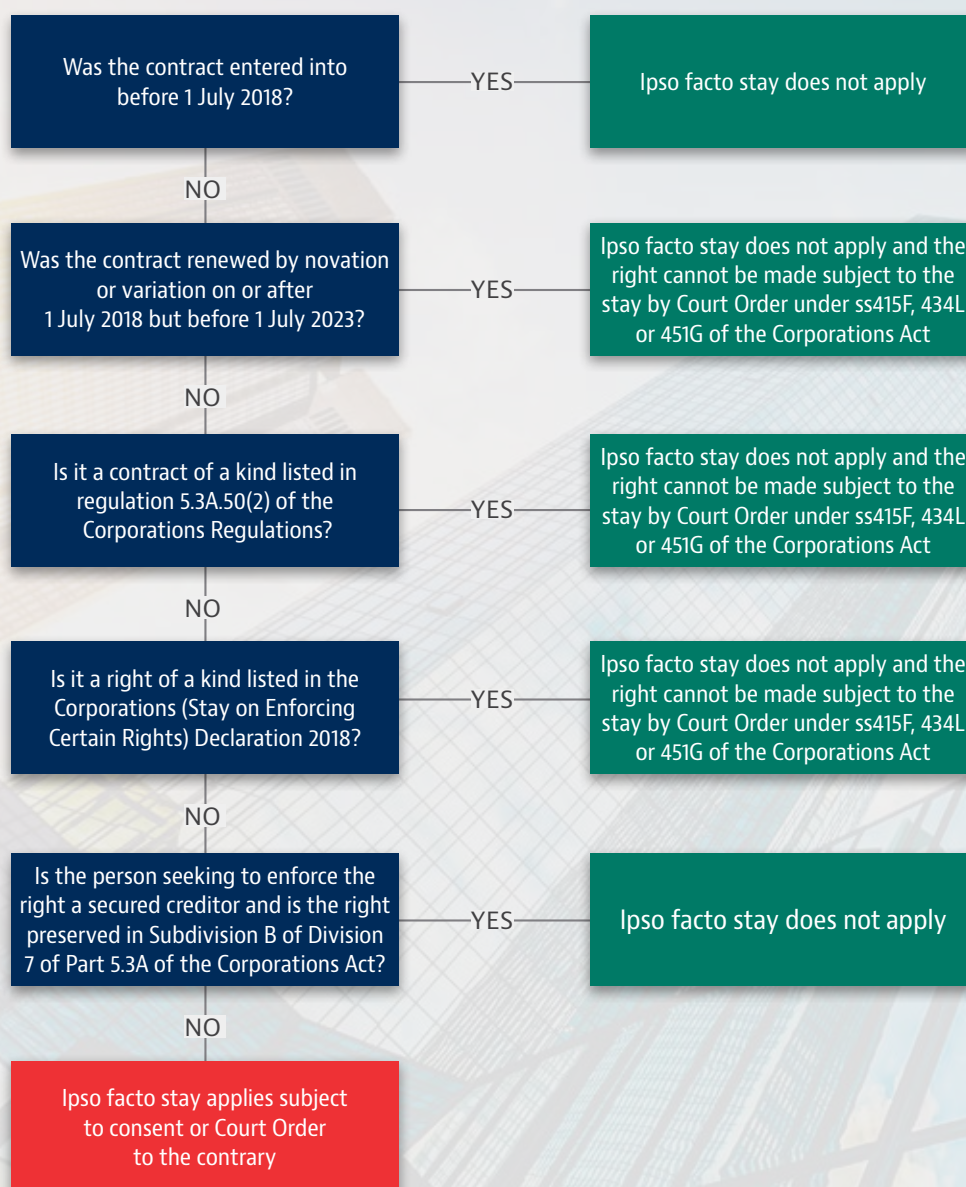
Exceptions to the stay

The ipso facto stay does not operate in a blanket manner, and there are various exceptions to the stay. These exceptions include the following statutory exceptions:

1. a right under a contract entered into after the relevant insolvency event;
2. certain rights of secured creditors in an administration, including:
 - (a) the right to appoint a receiver over the whole or substantially the whole of the company's property during the "decision period";²
 - (b) the right of secured creditor who enforced before the administration commenced to continuing the enforcement;

² As defined in section 9 of the Act as being the day ending on the thirteenth business day after the commencement of the voluntary administration or the giving of notice of the appointment of the voluntary administrator to the secured party.

Ips0 facto stay decision tree*



* Assumes an ipso facto contractual right exists and the counterparty has entered a specified insolvency procedure

- (c) the right of a secured creditor to enforce against perishable property; and
 - (d) the right to give a notice under a security agreement;
3. where the court lifts the stay (which it can do so if it is appropriate in the “interests of justice”); and
 4. where the stay is lifted with the consent of the scheme administrator, receiver or administrator (as applicable).

In addition, to the above, certain types of contracts or rights may also be specifically excluded from the stay.

Where a type of contract is excluded from the stay all rights under that contract are excluded from the operation of the stay. By contrast, where a certain type of right is excluded, that right is excluded from the stay irrespective of the type of contract it is contained in.

A full list of the types of contracts that have been excluded can be found in Regulation 5.3A.50(2) of the *Corporations Regulations 2001* (Cth) (Regulations) and a full list of the types of rights that have been excluded from the stay can be found in the *Corporations (Stay on Enforcing Certain Rights) Declaration 2018* (Declaration), as amended. A consolidated list of excepted contracts and rights provided for in the Regulations and the Declaration are set out at the end of this document.

Exclusions¹ from the Ipso Facto provisions² inserted into the *Corporations Act 2001* (Act) with effect from 1 July 2018

The kinds of contracts, agreements or arrangements which are excluded²

Arrangements relating to laws, international obligations and public services *

- (a) an agreement (within the meaning of the **Convention** defined in section 3 of the *International Interests in Mobile Equipment (Cape Town Convention) Act 2013*)
- (b) a contract, agreement or arrangement that is a licence, permit or approval issued by:
 - (i) the Commonwealth, a State or a Territory; or
 - (ii) an authority of the Commonwealth or of a State or a Territory; or
 - (iii) a local governing body established by or under a law of a State or Territory
- (c) a contract, agreement or arrangement relating to Australia's national security, border protection or defence capability
- (d) a contract, agreement or arrangement for the supply of goods or services to a public hospital or a public health service
- (e) a contract, agreement or arrangement for the supply of goods or services by or on behalf of a public hospital or a public health service
- (f) a contract, agreement or arrangement for the supply of essential or critical goods or services to, or the carrying out of essential or critical works for:
 - (i) the Commonwealth, a State or a Territory; or
 - (ii) an authority of the Commonwealth or of a State or a Territory; or

- (iii) a local governing body established by or under a law of a State or Territory; or
- (iv) the public on behalf of an entity covered by subparagraph (i), (ii) or (iii)

Note: Examples of these essential or critical goods, services or works include public transport services, public security or safety services, and works affecting essential public infrastructure.³

Arrangements relating to securities and financial products *

- (g) a contract, agreement or arrangement that is, or is directly connected with, a derivative
- (h) a contract, agreement or arrangement that is, or is directly connected with, a securities financing transaction
- (i) a contract, agreement or arrangement for the underwriting of an issue, or sale, of securities, financial products, bonds, promissory notes, or syndicated loans
- (j) a contract, agreement or arrangement under which a party is or may be liable to subscribe for, or to procure subscribers for, securities, financial products, bonds, promissory notes, or syndicated loans
- (k) a contract, agreement or arrangement that is, or governs, securities, financial products, bonds, promissory notes, or syndicated loans
- (l) a contract, agreement or arrangement under which securities are offered, or may be offered, under a rights issue

¹ This document summarises the regulations and declarations made for the purposes of sections 415D, 434J and 451E of the Act in effect as at 1 September 2018. Each of sections 415D, 434J and 451E should be read in their entirety in order to fully understand the operation of the new ipso facto prohibition, and the exclusions from it, which extend beyond those summarised in this document. Sourced from the Federal Register of Legislation at 10 September 2018. For the latest information on Australian Government law please go to <https://www.legislation.gov.au>. Reproduced under the [Creative Commons licence](https://creativecommons.org/licenses/by/4.0/legalcode) (creativecommons.org/licenses/by/4.0/legalcode) governing the use of federal legislation.

² Contained in 5.3A.50(2) of the *Corporations Regulations 2001* inserted with effect from 1 July 2018 by the *Corporations Amendment (Stay on Enforcing Certain Rights) Regulations 2018*.

³ Note that paragraph (f) of Corporations Regulation 5.3A.50(2) was amended by the *Corporations Amendment (Stay on Enforcing Certain Rights) Regulations (No.2) 2018*.

* Headings appear in the Explanatory Statement to the Regulations, but not actually in the Regulations.

- (m) a contract, agreement or arrangement for the sale of all or part of a business, including by way of the sale of securities or financial products
- (n) a contract, agreement or arrangement for the issue of an instrument that:
 - (i) is a security, financial product, bond, promissory note, or syndicated loan; and
 - (ii) belongs to a class of such instruments, each of which is fungible, and the first of which was issued before 1 July 2018
- (o) a contract, agreement or arrangement that is, or is directly connected with, a margin lending facility (within the meaning of Chapter 7 of the Act)
- (p) a contract, agreement or arrangement that is:
 - (i) a covered bond (within the meaning of the *Banking Act 1959*); or
 - (ii) for issuing such a bond; or
 - (iii) directly connected with such a bond or the issuing of such a bond

Complex arrangements between sophisticated parties *

- (q) a contract, agreement or arrangement providing for the management of financial investments
- (r) a contract, agreement or arrangement that involves a special purpose vehicle, and that provides for securitisation or a public-private partnership
- (s) a contract, agreement or arrangement that involves a special purpose vehicle, and that provides for a project finance arrangement under which:
 - (i) a financial accommodation is to be repaid or otherwise discharged primarily from the project's cash flow; and
 - (ii) all or substantially all of the project's assets, rights and interests are to be held as security for the financial accommodation
- (t) a contract, agreement or arrangement for the keeping in escrow of:
 - (i) code, or passwords, for computer software; or
 - (ii) material directly associated with such code or passwords
- (u) a contract, agreement or arrangement for the commercial charter of a ship if:
 - (i) the ship is not an Australian ship (within the meaning of the *Shipping Registration Act 1981*); and
 - (ii) the charter is by an Australian national (within the meaning of that Act) for the purposes of exporting goods from Australia, or from an external Territory, to another country

Arrangements relating to debt and the ranking of creditors *

- (v) a contract, agreement or arrangement under which the priority of security interests in particular property is changed or can change
- (w) a contract, agreement or arrangement that is a flawed asset arrangement
- (x) a contract, agreement or arrangement that is, or is directly connected with, a factoring arrangement (within the meaning of the *ASIC Corporations (Factoring Arrangements) Instrument 2017/794*)

Arrangements relating to financial markets, and clearing and settlement facilities *

- (y) a contract, agreement or arrangement that is the operating rules (other than the listing rules) of a financial market;

Note: The operating rules of a licensed market (within the meaning of Chapter 7 of the Act) are a contract, see subsection 793B(1) of the Act.
- (z) a contract, agreement or arrangement that is the operating rules of a clearing and settlement facility

Note: The operating rules of a licensed CS facility (within the meaning of Chapter 7 of the Act) are a contract, see subsection 822B(1) of the Act
- (za) contract, agreement or arrangement that confers rights on the operator of a financial market, or the operator of a clearing and settlement facility, in relation to the operation of the market or facility
- (zb) contract, agreement or arrangement of which the parties include the Reserve Bank of Australia and the operator of a clearing and settlement facility
- (zc) a contract, agreement or arrangement under which participants (within the meaning of Chapter 7 of the Act) in a clearing and settlement facility may settle obligations on behalf of other participants (within the meaning of that Chapter) in the facility

RTGS systems and netting arrangements within the operation of the *Payment Systems and Netting Act 1998* *

- (zd) a legally enforceable arrangement referred to in paragraph 9(1)(b) of the *Payment Systems and Netting Act 1998* that supports an approved RTGS system (within the meaning of that Act)

Note: The arrangement includes the rules that are part of that arrangement.
- (ze) an approved netting arrangement (within the meaning of the *Payment Systems and Netting Act 1998*);

Note: The arrangement includes the rules that are part of that arrangement.
- (zf) a contract, agreement or arrangement that confers rights on:
 - (i) the operator of an approved RTGS system (within the meaning of the *Payment Systems and Netting Act 1998*); or
 - (ii) the coordinator of an approved netting arrangement (within the meaning of that Act);
 in relation to the operation of that system or netting arrangement
- (zg) a contract, agreement or arrangement under which the parties to an arrangement covered by paragraph (zd) or (ze) (the *main arrangement*) may settle obligations on behalf of other parties to the main arrangement
- (zh) a close-out netting contract (within the meaning of the *Payment Systems and Netting Act 1998*)
- (zi) a contract, agreement or arrangement under which security is given over financial property (within the meaning of the *Payment Systems and Netting Act 1998*) in respect of eligible obligations (within the meaning of that Act) of a party to a contract covered by paragraph (zh)
- (zj) a netting market (within the meaning of the *Payment Systems and Netting Act 1998*)

* Headings appear in the Explanatory Statement to the Regulations, but not actually in the Regulations.

- (zk) a market netting contract (within the meaning of the *Payment Systems and Netting Act 1998*)
- (zl) a contract, agreement or arrangement under which security is given, in accordance with a market netting contract covered by paragraph (zk), in respect of obligations of a party to the market netting contract
- (zm) a contract, agreement or arrangement that is an outsourcing arrangement for the purposes of *Prudential Standard CPS 231 Outsourcing* or *Prudential Standard SPS 231 Outsourcing*
 Note 1: In 2018, *Prudential Standard CPS 231 Outsourcing* was set out in the *Banking, Insurance and Life Insurance (prudential standard) determination No. 6 of 2016*.
 Note 2: In 2018, *Prudential Standard SPS 231 Outsourcing* was set out in the *Superannuation (prudential standard) determination No. 3 of 2012*.

Arrangements prescribed for a certain period of time *

- (zn) a contract, agreement or arrangement entered into or renewed on or after 1 July 2018, but before 1 July 2023, as a result of either of the following:
- the novation of, or the assignment of one or more rights under, a contract, agreement or arrangement entered into before 1 July 2018;
 - a variation of a contract, agreement or arrangement entered into before 1 July 2018
- (zo) a contract, agreement or arrangement entered into on or after 1 July 2018, but before 1 July 2023, for the provision of any of the following kinds of work, goods or services for a particular project:
- building work (within the meaning of the *Building and Construction Industry (Improving Productivity) Act 2016*);
 - work to be carried out anywhere in Australia that, if carried out in New South Wales, would be covered by paragraph 5(1)(d) or (f) of the *Building and Construction Industry Security of Payment Act 1999 (NSW)* and not be excluded by subsection 5(2) of that Act;
 - goods or services to be provided anywhere in Australia that, if provided in New South Wales, would be related goods and services (within the meaning of the *Building and Construction Industry Security of Payment Act 1999 (NSW)*)
- if the total payments under all contracts, agreements or arrangements for the project for work, goods or services of those kinds is at least \$1 billion
- (zp) a contract, agreement or arrangement that:
- is entered into to enable the satisfactory completion of a contract, agreement or arrangement covered by paragraph (zo); and
 - is for the provision of a kind of work, goods or services covered by that paragraph.

The kinds of rights which are excluded⁴

- 5(4)(a) a right to change the basis, including by the application of a different rate, on which an amount in respect of or under any of the following is calculated:
- a financing arrangement;
 - a guarantee, indemnity or security related to a financing arrangement (whether or not the guarantee, indemnity or security is limited in any way)

where *financing arrangement* means:

- any form of financial accommodation; or
- a contract, agreement or arrangement of a kind known as a finance lease, an operating lease, a bill facility, a performance bond, a guarantee, a bank guarantee, a letter of credit or a hire purchase agreement

- 5(4)(b) a right to payment by way of indemnity (whether or not the indemnity is limited in any way) in respect of:
- any liability or loss arising as a result of a person preserving or enforcing rights; or
 - any charges and expenses incurred by a person in preserving or enforcing rights
- 5(4)(c) a termination right under a standstill or forbearance arrangement, whether or not the standstill or forbearance arrangement suspends, preserves or modifies the right under the other contract, agreement or arrangement to which it applies
 where *standstill or forbearance arrangement* means a contract, agreement or arrangement that suspends or restricts the enforcement of rights under another contract, agreement or arrangement
- 5(4)(d) a right to change the priority, or order, in which amounts are to be paid, distributed or received under a contract, agreement or arrangement
- 5(4)(e) a right of set-off or a right of combination of accounts
- 5(4)(f) a right to net balances or other amounts
- 5(4)(g) a right to take action to enforce:
- a right referred to in paragraph 5(4)(e) or (f); or
 - a right referred to in subsection 6(1), (2) or (3)⁵ if, on the enforcement of that right to take action, the circumstances referred to in subsection 6(4) or (5) (as applicable)⁶ would be satisfied;
- for the purposes of enforcing a right referred to in paragraph 5(4)(e) or (f), or in subsection 6(1), (2) or (3)⁶ (as applicable), whether or not an amount is due for payment, will or may become due for payment, or is unpaid;
- Note: The rights referred to in this paragraph include:
- a right to accelerate or otherwise vary a date for payment of an amount;
 - a right to convert or exchange amounts denominated in different currencies; and
 - a right to crystallise a security interest.
- 5(4)(h) a right to:
- assign or otherwise transfer rights or obligations; or
 - novate rights or obligations
- 5(4)(i) a right:
- for property that is subject to a circulating security interest to become subject to a non-circulating security interest; or
 - for a floating charge over property to operate as a fixed charge; or
 - for property consisting of accounts or chattel paper to be transferred to a secured party by way of security; or
 - that restricts the grantor of a security interest in property from dealing with the property
- where words and expressions that are defined for the purposes of the *Personal Property Securities Act 2009* have the same meanings

⁴ Contained in section 5(4) of the *Corporations (Stay on Enforcing Certain Rights) Declaration 2018*.

⁵ See below - these are *The kinds of rights which are excluded in specified circumstances*.

* Headings appear in the Explanatory Statement to the Regulations, but not actually in the Regulations.

5(4)(j) a right:
(i) to perform obligations; or
(ii) to engage another person to perform obligations; or
(iii) to enforce rights; or
(iv) to engage another person to enforce rights;
of the specified person under a contract, agreement or arrangement where *specified person* means the body, corporation or company the subject of subsection 415D(1), 434J(1) or 451E(1) of the Act (as applicable)

(4)(k) a right to enforce a possessory security interest in circumstances where paragraphs 440JA(b), (c) and (d) of the Act are satisfied where the reference to the company in paragraph 440JA(b) of the Act is taken to be a reference to the specified person and where *specified person* means the body, corporation or company the subject of subsection 415D(1), 434J(1) or 451E(1) of the Act (as applicable)

The kinds of rights which are excluded in specified circumstances⁶

6(4) A right to appoint a controller of property of the specified person in the following circumstances:⁷

- (a) the right is to be enforced by a person who has a security interest in, or over, property of the specified person; and
 - (b) in relation to property of the specified person:
 - (i) a controller has been appointed; or
 - (ii) a right to appoint a controller has been enforced
-

6(5) [Applicable in relation to creditors' schemes of arrangement only] A right to appoint a controller of property of the specified person in the following circumstances:⁸

- (a) the whole, or substantially the whole, of the property of the specified person is subject to a security interest; and
- (b) the right is to be enforced by the person who has the security interest referred to in paragraph (a).

⁶ Contained in subsections 6(4) and (5) of the *Corporations (Stay on Enforcing Certain Rights) Declaration 2018*.

⁷ See subsections 6(1), (2) and (3) of the *Corporations (Stay on Enforcing Certain Rights) Declaration 2018*.

⁸ See subsection 6(1) of the *Corporations (Stay on Enforcement of Certain Rights) Declaration 2018*.

* Headings appear in the Explanatory Statement to the Regulations, but not actually in the Regulations.

Contacts

Maria O'Brien

Partner

+61 2 8922 5222

maria.obrien@bakermckenzie.com

Peter Lucarelli

Partner

+61 3 9617 4407

peter.lucarelli@bakermckenzie.com

David Walter

Partner

+61 2 8922 5294

david.walter@bakermckenzie.com

Ian Innes

Special Counsel

+61 7 3069 6217

ian.innes@bakermckenzie.com

Heather Sandell

Special Counsel

+61 2 8922 5514

heather.sandell@bakermckenzie.com

Adam Jeffrey

Special Counsel

+61 2 8922 51956

adam.jeffrey@bakermckenzie.com

Kevin Shum

Associate

+61 2 8922 5181

kevin.shum@bakermckenzie.com

Cal Dioluín

Associate

+61 2 8922 5522

cal.dioluin@bakermckenzie.com

Angus Napier

Associate

+61 2 8922 5180

angus.napier@bakermckenzie.com



Baker McKenzie helps clients overcome the challenges of competing in the global economy.

We solve complex legal problems across borders and practice areas. Our unique culture, developed over 70 years, enables our 13,000 people to understand local markets and navigate multiple jurisdictions, working together as trusted colleagues and friends to instill confidence in our clients.

Baker McKenzie.

bakermckenzie.com

This document is a summary only of the law as at 1 March 2020 and has been prepared for the general information of clients and/or professional associates of Baker & McKenzie. You should not rely on the contents. It is not legal advice and should not be regarded as a substitute for legal advice. To the fullest extent allowed by law, Baker & McKenzie excludes all liability (whether arising in contract, negligence or otherwise) in respect of all and each part of this communication, including without limitation, any errors or omissions.

Baker & McKenzie, an Australian Partnership, is a member firm of Baker & McKenzie International, a global law firm with member law firms around the world. In accordance with the common terminology used in professional service organizations, reference to a "partner" means a person who is a partner or equivalent in such a law firm. Similarly, reference to an "office" means an office of any such law firm. This may qualify as "Attorney Advertising" requiring notice in some jurisdictions. Prior results do not guarantee similar outcomes.

© 2020 Baker & McKenzie. All rights reserved.