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**Pre-packaged Administrations in the UK:**

**Nothing new under the Sun!**

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*Introduction*

The English corporate insolvency framework has gone through significant changes in recent times. Some of these changes have been introduced as soon as the effects of the COVID-19 pandemic on the UK economy became apparent. Nevertheless, last summer the *Corporate Insolvency and Governance Act 2020* (the Act), which completed its progress in the Parliament and received Royal Assent on 25 June 2020, coupled these temporary measures with long-term reforms and regulatory powers to significantly amend the UK corporate insolvency framework.

Similar to other countries, the UK introduced some emergency legislation aimed at suspending statutory demands and restricting winging-up petitions,[[1]](#footnote-1) as well as the liability for wrongful trading.[[2]](#footnote-2) At the same time, with the Act, Parliament took the opportunity to introduce some long-discussed and more permanent changes to the corporate insolvency framework. These include the introduction of a short free-standing company moratorium,[[3]](#footnote-3) a new restructuring plan procedure (known as “part 26A restructuring plan”) modelled after the successful schemes of arrangement (but with a cross-class cram-down!),[[4]](#footnote-4) and a general ban on the enforceability of *ipso facto* clauses.[[5]](#footnote-5)

*Classic Administration*

It seems, therefore, that the country – or at least its legislator – is trying to replace or, at least, discourage the use of the formal insolvency procedure originally designed to promote the rescue of distressed yet viable companies. This is the administration procedure governed by Schedule B1 of the *Insolvency Act 1986*, as amended by the *Enterprise Act 2002*.

There is, in fact, a widespread belief that this procedure is inadequate to achieve the goals for which it was introduced. These are: rescuing the company as a going concern, achieving a better result than liquidation or, in the last instance, realising the company’s assets to make a distribution.[[6]](#footnote-6) For instance, media outlets frequently depict administration as “the end of the road” for the debtors by reporting on companies “collapsing” into administration.[[7]](#footnote-7)

To be fair, for some companies, administration is the end of the road. This seems to be the case of one of the most illustrious administration cases of this year, Philip Green’s Arcadia group collapse into administration.[[8]](#footnote-8) In the case of Arcadia, it is quite likely that the doors of the stores of the retail group will never open again. Its most iconic brands are being sold to online retailers,[[9]](#footnote-9) and the company’s 13,000 employees are going to be jobless in the next few weeks.

However, it appears a bit too premature to call for the demise of administration as a valid and efficient tool for rescuing companies and/or turning around their business. This opinion seems to be shared by Parliament which, back in June 2020, granted to the Government an extension to the end of June 2021 to the power to legislate on pre-packaged sales to connected persons. This legislative power was originally granted by the *Small Business, Enterprise and Employment Act 2015*, but later expired in May 2020.[[10]](#footnote-10)

*Proposals for Pre-packaged Administrations*

At the time of writing, it seems that the Government is willing to legislate in the area before the extended deadline expires. In fact, on 8 October 2020, the UK Government published draft regulations[[11]](#footnote-11) aimed at pre-packaged sales to connected parties which occur by means of an administration proceeding. The term “pre-packaged sale” refers to an arrangement under which the sale of all or part of a company’s business or assets is negotiated with a purchaser prior to the appointment of an administrator and the administrator effects the sale immediately on, or shortly after, appointment.[[12]](#footnote-12)

According to the legislative proposal, where an administrator wishes to dispose of all or a substantial part of a company’s assets within the first eight weeks of the administration to one or more connected persons, then the administrator will need to obtain the creditors’ approval or an independent written opinion by an “evaluator”. This written opinion will be made available to the creditors and a copy will need to be filed at Companies House.

The provider of the opinion (referred to in the regulations as the “evaluator”) must be independent of the connected party purchaser, the company and the administrator, and must meet certain eligibility requirements. In the past, such opinions were provided by an independent body of business experts known as the “Pre-Pack Pool” (“the Pool”).[[13]](#footnote-13) However, the Pool has so far suffered from a low uptake rate of referrals, mainly due to the voluntary nature of such referrals by the connected party purchaser. Additionally, the Pool has wrongly been perceived as inadequate to identify bad deals. This bad publicity primarily generated from the unfair reports on the *Polestar* case, where the pre-pack sale fell through for reasons that had nothing to do with the “positive” opinion[[14]](#footnote-14) on the pre-pack sale given by the Pool.[[15]](#footnote-15)

It seems, therefore, unlikely that the Government will rely solely on the Pool for this role. In fact, section 9 of the draft regulations refers to the evaluator as “an individual”, not as a body of experts. Nevertheless, nothing seems to suggest that evaluators could not join independent bodies in order to gain visibility and promote their services on the market. The Pool may, therefore, end up in being one of the evaluators, rather than the only one (as it is the situation today).

It is clear that, with these draft regulations, the Government is trying to introduce additional checks and balances in an area where there is a widespread perception of abusive or at least strategic behaviour from businesses. In particular, the Government is concerned that these practices could result in mechanisms to avoid tax and pension liabilities.[[16]](#footnote-16)

It is arguable whether the negative perception around pre-packs, and especially those to connected parties, always reflects the reality. The author is not aware of any recent empirical studies, which suggest an increased use of pre-packs in a strategic or abusive manner. At least, in this context, it is reassuring that the Government, through its Insolvency Service, has not chosen to completely ban pre-packs (despite having such power in light of the Act). It is encouraging that the Government has recognised that pre-packaged sales in administration are a valuable rescue tool in the restructuring toolbox, especially in the current economic and financial situation. For instance, *Paperchase* was recently successfully rescued in a pre-pack deal to a connected party (*Permira Debt Managers*, an investor in *Paperchase* since 2015), thus safeguarding around 1,000 jobs in the hard-hit retail sector.[[17]](#footnote-17)

It is questionable whether and to what extent the draft regulations will address the concerns they are designed to alleviate. Their scope may be too broad and there is little clarity on the potential liability of the evaluator in case of perceived mistake (see the *Polestar* case). With reference to the qualifying criteria to be an evaluator, these have proved particularly controversial in the industry, with some believing that they could open the door to abuse of the system.[[18]](#footnote-18)

It is not clear on which basis the creditors’ opinion could be independently formed in the absence of a report from the evaluator. Additionally, it seems unlikely that creditors will be frequently asked to validate a pre-pack deal, as at least 14 days prior notice is required for their approval. This rather lengthy notice period – if not amended in the final version of the law - jeopardises the main benefits (speed and efficiency) associated with pre-pack sales.

Finally, while the administrator could in theory ignore the evaluator’s opinion, it is difficult to see how an officer of the court could act against the advice of an independent expert. Furthermore, the position of secured creditors in these deals need to receive further attention. A note within the government's report suggests that pre-pack sales to a secured lender to the company will not be caught by the regulations. However, the draft regulations do not expressly include any such exemption at this time.

*Summary*

Overall, this draft legislation seems to strike a balance between the interests of the parties involved in a sale, as well as promote transparency and disclosure in potentially murky deals. It is essential that the newly proposed mechanisms do not result in additional costs and delays for the parties of the proposed deals. At the risk of stating the obvious, it is worth remembering that time and money are of the essence for all companies, but particularly those finding themselves in a situation of financial distress.

1. Sections 10-11 of the Act. [↑](#footnote-ref-1)
2. Sections 12-13 of the Act. [↑](#footnote-ref-2)
3. Sections 1-6 of the Act. [↑](#footnote-ref-3)
4. Schedule 9 to the Act. [↑](#footnote-ref-4)
5. Sections 14-19 of the Act. [↑](#footnote-ref-5)
6. Paragraph 3, Schedule B1 IA 1986. [↑](#footnote-ref-6)
7. By way of example, see: S. Butler, “Carluccio’s and BrightHouse collapse into administration” (*The Guardian*, 30 March 2020); S. Butler, “Oasis and Warehouse close to collapsing into administration” (*The Guardian*, 14 April 2020); S. Butler, “Peacocks and Jaeger businesses collapse into administration” (*The Guardian*, 19 November 2020). [↑](#footnote-ref-7)
8. S. Butler and J. Partridge, “Philip Green’s Arcadia Group collapses into administration” (*The Guardian*, 30 November 2020). [↑](#footnote-ref-8)
9. M. Sweeney and Z. Wood, “Boohoo in talks to buy Dorothy Perkins, Wallis and Burton” (*The Guardian*, 29 January 2021);K. Makortoff, “Asos buys Topshop and Miss Selfridge brands for £330m” (*The Guardian*, 1 February 2021). [↑](#footnote-ref-9)
10. Section 8 of the Act. [↑](#footnote-ref-10)
11. Draft *Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2020*, available at: <https://www.gov.uk/government/publications/pre-pack-sales-in-administration>. [↑](#footnote-ref-11)
12. Statement of Insolvency Practice 16. [↑](#footnote-ref-12)
13. See: < https://www.prepackpool.co.uk/>. [↑](#footnote-ref-13)
14. In reality, the Pool does not state if the sale should go through. It only states if the case for a sale to a connected party is not unreasonable, unreasonable or if additional evidence is needed. [↑](#footnote-ref-14)
15. J. Francis, “Polestar sites go into administration” (*Printweek*, 25 April 2016). [↑](#footnote-ref-15)
16. L. Haddou and J. Cumbo, “Companies use ‘pre-packs’ to dump £3.8bn of pension liabilities” (*Financial Times*, 9 April 2017). [↑](#footnote-ref-16)
17. J. Bourke, “Paperchase to keep majority of its shops open, safeguarding around 1,000 jobs” (*Evening Standard*, 29 January 2021). [↑](#footnote-ref-17)
18. J. Hillman, “Compulsory independent scrutiny of pre-pack sales to connected parties” (*Pinsent Masons*, 22 October 2020), available at: <https://www.pinsentmasons.com/out-law/analysis/compulsory-independent-scrutiny-pre-pack-sales-connected-parties>. [↑](#footnote-ref-18)