

Approaches to Insolvencies of Wide Public Impact

Rebecca Parry

Professor, Nottingham Law School,
Nottingham Trent University

Overview

There is a creditor focus in typical insolvency procedures

However, some cases have wide public impact and approaches to such cases vary, including

- Special insolvency procedures

- Other ad hoc means of state intervention

- Bailouts/bail-ins

Focus is on strategically important non-financial enterprises, “SINFIs”

Theoretical Foundations

- A ‘creditors’ bargain’ approach has the benefit of clarity and predictability for creditors, based on pre-existing entitlements. Wider concerns are to be dealt with outside of insolvency law.
- Stakeholder approaches identified the narrowness of this approach, given that insolvencies can have wider impacts. Potentially suffer from unpredictability.
 - Insolvencies of wide public interest provide an example of a case where it may be appropriate to focus not only on the interests of creditors.

EU Restructuring Directive

- EU Directive on Preventative Restructuring Frameworks, 2019/23,
 - Recital 11, notes potential for “the so-called domino effect of insolvencies”
 - Excludes various types of financial entity e.g. insurance companies, credit institutions
 - Also excludes public bodies under national law
- ...but the directive does not otherwise address the issue of SINFI.

Contrast: EU Financial Sector

- Briefly, by way of contrast:
 - Extensive macroprudential preventative legislation as well as special insolvency procedures in view of systemic risk.
- In contrast most non-financial firms fall outside similar frameworks given a lack of systemic risk (although tech provides one exception on both counts).

Context: Nonfinancial Sector

- Increasing role of private companies in delivering essential services to the public in the UK (and other jurisdictions).

Private Sector Suppliers of Public Services

Privatised, former state-owned enterprises

Various alternative service delivery models

Outsourcing

Strategic suppliers

Universities and colleges

Charities

UK Privatisations

- UK, Thatcher government
 - 1979-81 initial focus on reducing public sector borrowing, privatisation of British Aerospace and Cable & Wireless
 - 1982-86 extensive privatisations including British Gas and British Telecom
 - 1987-96 water and electricity, British Steel, British Rail, electricity generation
- Subsequently privatisations continued.
 - 1997-2008 Private Finance Initiative, non-core privatisations of Horseracing Totaliser and Channel Tunnel
 - 2009 onwards Royal Mail. Increased uses of private sector to deliver public provision in NHS.

EU Member State Privatisation Examples

- Germany – long history, initially e.g. Volkswagen to encourage stock market investment by individuals, later to improve efficiency.
- Spain, privatisation in 1980s onwards; Italy in 1990s onwards; Greece, early 1990s onwards
- France, greater ambivalence but patterns of privatisation post-1986

Perceived Benefits of Privatisation

- One reason is that exposure to market forces is expected to bring efficiencies through incentives and improved information flows.
 - However, there is commonly identified potential for market failures e.g. monopolies, externalities, need for public goods and services.
 - These factors are magnified in the case of SINFIIs e.g. situational monopolies of health care providers.
 - Insolvencies are a risk, as well as an incentive for efficiency, in any market-based system.

Other Nonstate Examples

- Greater reliance on technologies provided by digital service firms which have always been non-state sector, some of which have been noted as having “too big to fail” potential.

Public Impact of “SINFI” failures

- Loss of service to consumers
 - Likely to be difficulties in arranging alternative supplies.
- Impacts on employees, communities and the environment

Preventative Measures

- Network and Information Systems Regulations 2018 SI 2018/506rective (EU) 2016/1148 of the European Parliament and of the Council of 6 July 2016 concerning measures for a high common level of security of network and information systems across the Union
 - Security and resilience (cyber and physical) of digital services and essential services.
- Strong failure prevention proactivity but reactive approaches are needed also for when failure occurs.

Approaches to SINFI Insolvencies

- Bailouts
- Renationalisations
- Mainstream insolvency procedures
- Bespoke sectoral insolvency procedures
- Large company insolvency procedures
- Ad hoc closure approaches

Bailouts

- Examples in banking sector in response to 2008 crisis “too big to fail” concerns. Subsequent emphasis on macroprudential approaches.
- Non-financial examples in health sector –vulnerability of users and effective situational monopolies that arises as result.
- Subject to EU state aid restrictions.
- Create moral hazard problems. Encourage excessive lending and risky behaviour. Sub-optimal investment decisions.

Renationalisation

- Examples recently involving energy companies in France and Germany

Mainstream Insolvency Procedures

- IA 1986, Sch B1, Administration e.g.
 - Energy suppliers,
 - Monarch Airline,
 - Harland and Wolff
- Existing management can assist with complexities
- Risks for office holder

Sectoral Insolvency Procedures (Nonfinancial)

- Water Industry Act 1991, supplemented by with the Water Industry (Special Administration) Rules 2009, SI 2009/2477.
- Railways Act 1993, ss 59-65, supplemented by the Railway Administration Order Rules 2001, SI 2001/3352
- Transport Act 2000, ss 26-32 (air traffic control).
- Postal Services Act 2011, ss 68-88;
- Housing and Planning Act 2016, Chapter 5 (social housing).
- Technical and Further Education Act 2017, Chapter 4 ETC.

Example, UK Energy Sector

- Energy Act 2011, s 94, supplemented by the Energy Supply Company Administration Rules 2013, SI 2013/1046.
 - Aim is prevent market contagion, maintain market stability and protect customers.
 - Energy suppliers buy energy wholesale and sell it on to customers.
 - Diverse suppliers got into difficulties. Preference is for contracts to be transferred to other suppliers.
 - Only one supplier, Bulb, has as yet gone into special administration.

Other Sectoral Approaches

- Some sectors do have regulatory requirements that would protect customers or investors in the event of insolvency e.g.
 - Levies to support insolvency resolution (airlines)
 - Wind-down arrangements (crowdfunding)
- Tech sector has a history of responding collectively to provide solutions to new viruses but might not respond in the same way in an insolvency.

Large Company Insolvency Procedures

- Italy – extraordinary administration for large enterprises
- Croatia – *Zakon o postupku izvanredne uprave u trgovačkim društvima od sistemskog značaja za Republiku Hrvatsku* “Act on Extraordinary Administration Proceedings in Companies of Systemic Importance for the Republic of Croatia”, “Lex Agrokor”
- Subsequent similar approach in Slovenia, “Lex Mercator”.

Ad Hoc Approaches

- Compulsory liquidations, controlled by Official Receiver
 - British Steel
 - Carillion
 - Thomas Cook
 - *Re Baglan Operations Ltd* [2022] EWHC 647 (Ch)

Liquidation

- IA 1986, s 143 the functions of a liquidator of a company which is being wound up by the court are "to secure that the assets of the company are got in, realised and distributed to the company's creditors, and, if there is a surplus, to the persons entitled to it"
 - Re Pantmaenog Timber Co Limited [\[2004\] 1 AC 158](#) per Lord Millett at [63]-[64] allows public interest considerations.
- Powers of liquidator under IA 1986, Sch 4, para. 5 Paragraph 5 "Power to carry on the business of the company so far as may be necessary for its beneficial winding up."

Liquidator's Duties

- Liquidation – IA 1986, Sch 4, para 5 permits ongoing trading to enable a “beneficial winding up”

Liquidator's Duties, Cases

- Consistent case law in which the environment has been regarded as an important consideration alongside the interests of creditors.
 - *Re Mineral Resources Ltd* [1999] BCC 422
 - *Re Rhondda Waste Disposal Ltd* [2001] Ch 57
- Ex Parte James [1874] LR 9 Ch App 609 as explained by David Richards LJ in Lehman Brothers Australia Limited v MacNamara [2020] EWCA Civ 321 at [35] as "the standards which right-thinking people...would think should govern the Court or its officers".

Recent Case

- *Re Baglan Operations Ltd* [2022] EWHC 647 (Ch)
 - Official Receiver could take into account ‘the potential detriment to the locality - the Company's "beneficial" winding up being one conducted to the advantage of those in whose interest it was being undertaken (who were not exclusively the creditors)’.
 - Concerns that winding up should be done in a safe manner.

Uncertainties of Current Law

- Although there is recognition in existing case law that the public interest can be accommodated, the extent of this in non-environmental cases is not yet known.

Possible Approaches

- Focus on protection of functions but not of entities if non-viable.
- Offer market-based approaches such as bail-ins where there is underlying viability.
- Clearer statutory provision could be of benefit.
 - Special insolvency procedures for key sectors (precise but risks of being under-inclusive).
 - A broader insolvency procedure for SINFI, offering financial safeguards, subject to ministerial discretion (flexible but risks of uncertainty in application)
 - A more general power to modify the objectives of office holders in SINFI cases (principles based, potentially uncertain).