

What's happening in insolvency? Developments and how they might affect you

Dr Sandra Frisby
Baker & McKenzie Associate Professor and Reader in Company and
Commercial Law
University of Nottingham

CC-R Interactive Conference
6 October 2009

More on Pre-packs!

- A pre-pack is the sale of an insolvent company's business, commonly negotiated by an administrator prior to appointment and executed immediately after that appointment
- Pre-packs are becoming increasingly common
 - The Insolvency Service predicts that 1,250 pre-packs will take place this year
- They have attracted the interest of the media
 - Coverage is largely negative, especially where the business is purchased by its existing owner/managers
 - Cobra Beer, USC, The Officers Club *et al...*

Why the Controversy?

- The phoenix rising from its own ashes?
 - Pre-packs more commonly involve sales to ‘connected’ parties than other forms of sale
 - By far the most common complaint amongst trade creditors
- Conspiracy theories
 - Creditor suspicion about collusion between practitioners, purchasers, management, owners, secured creditors etc.
- Bias against financial interests of trade creditors
 - In the run-up to insolvency and in fixing the price to be paid for the business
- The “done deal”
 - Another common complaint: it all happens without, or with very limited, creditor involvement

The Profession's Response: SIP 16

- Commissioned by the Joint Insolvency Committee, produced by the Association of Business Recovery Professionals (R3) and approved and adopted by all regulatory bodies
- In force as from 1 January 2009
- Designed to increase the transparency of the pre-pack strategy
- Applicable to all pre-pack sales taking place through the administration procedure (so not receivership sales or liquidation sales)

SIP 16: *ex ante* creditor protection

- Who is the practitioner advising or acting for in the pre-appointment period?
 - Advice for the company is not the same thing as advice for *its directors* (para.5)
 - Directors should therefore be independently advised (particularly if they are hoping to purchase the business)
- Incurring credit in the pre-appointment period
 - Remember wrongful trading! Section 214 Insolvency Act 1986 (para.6)
- Taking account of creditor interests
 - Projecting post-appointment obligations into the pre-appointment period. Duty to perform functions in interests of creditors generally and not to unnecessarily harm their interests under para.3(2) and (4) of Schedule B1 Insolvency Act 1986 (para.7)

SIP 16: *ex post* disclosure requirements (para.9)

- 'Pre-pre-pack' process (?!)
 - Source of introduction, extent of involvement, marketing activities and valuation advice
- The 'thought process'
 - Alternatives considered, why no post-commencement campaign, whether funding requested and details of consultations with creditors
- The sale
 - Date, what was sold, price, terms of contract, purchaser (and connections to insolvent company), existence of guarantees in favour of financiers and those financiers' involvement with Newco
- When to disclose?
 - "...this information should be provided with the first notification to creditors", or at initial creditors meeting or in statement of proposals (para. 11)

So how good is it?

- In the event of proper compliance, highly informative to creditors
 - Addresses the ‘transparency gap’
 - Reassures creditors of the propriety or the necessity of the pre-pack?
 - Explains (convincingly?) why you lost money
 - Hey, that’s insolvency for you....”
 - *Might* assist with decisions about whether to trade with Newco or not

Proper compliance? The Insolvency Service tracking

- 572 pre-pack reports reviewed by the IS
 - 65% fully compliant with SIP 16
 - Most common weakness is failure to deal with marketing/valuation issues: recommended that more information provided
 - More information on justification for the pre-pack also recommended
 - Timing of reports to creditors
 - Generally good, but should 'day one' reports be the norm?
 - The hotline
 - Handles pre-pack complaints through the Investigations and Enforcement Services and the Companies Investigations Branch
 - Too early to know the outcome, but relatively small number of investigations ongoing
 - Tracking ongoing
 - IS to report again early in 2010

Good news for creditors?

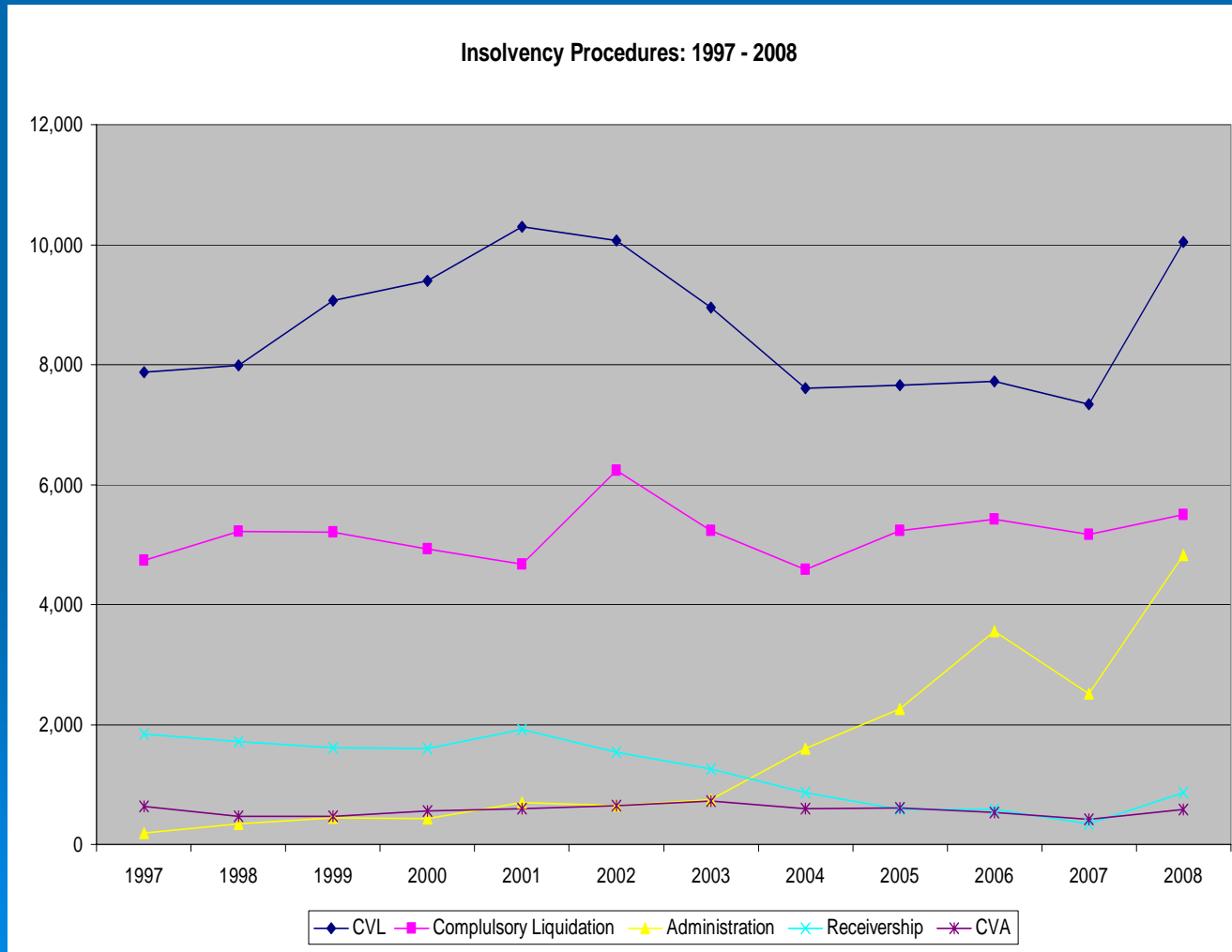
➤ In essence, yes

- Much better information should be provided
- Process is now independently monitored
- And SIP 16 information can be useful to creditors after the event

➤ But SIP 16 is not a pre-pack panacea

- As a matter of policy, should the phoenix syndrome be considered?
 - Bears emphasis that this is not exclusively a pre-pack phenomena!

And now for something completely different...



Doing more to rescue companies

➤ The Insolvency Service Consultation

- Promoting the rescue culture
 - Rescue of *companies* and not simply recycling businesses
- Beefing up the CVA and administration procedures
 - Extension of CVA with moratorium to medium and large companies (currently only available to small companies)
 - Super-priority finance contemplated

Implications?

- Very difficult to predict!
 - Super-priority finance *may* rescue more companies
 - Leaving customers intact for future trading
 - If the rescue fails, trade creditors are one step further down the payment ladder
- Interesting times ahead then!