Pre-pack administrations

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Summary

What is a pre-pack?

A “pre-pack” is 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 the administrator, and the sale contract executed on the appointment of the administrator or very shortly afterwards.

When used appropriately, a pre-packaged administration (“a pre-pack”) can be an effective company rescue procedure. Pre-packs enable the sale of company assets to be undertaken quickly (reducing the likelihood of important contracts being lost), preserving the brand and the value of the business and, ultimately, returns for creditors. However, there are concerns about the transparency of the pre-pack administration procedure, in particular:

- where businesses are being sold to “connected parties” (i.e. directors, shareholders and others connected with the insolvent company);
- possible conflicts of interest for the insolvency practitioner (for instance, when appointed by the floating charge-holder); and
- a lack of involvement of unsecured creditors.

To address these concerns, a Statement of Insolvency Practice (SIP 16) was issued in January 2009 (and periodically updated), with additional measures being introduced on 31 March 2011. The current SIP 16 came into force on 1 November 2015.

Following the publication of a Select Committee report in February 2013, the Government announced in July 2013 an independent review of the pre-pack procedure. The Graham Review into Pre-Pack Administration was published in June 2014 alongside Pre-Pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration by the University of Wolverhampton. Responding to Teresa Graham’s report, the Government said that it supported a voluntary approach and would work with business and industry to implement in full her six recommendations. A key recommendation, the introduction of a Pre-Pack Pool of independent experts to give an opinion on a proposed pre-pack sale to a “connected party” (if requested to do so), became operational on 2 November 2015.

The Small Business Enterprise and Employment Act 2015 (SBEEA 2015), which received Royal Assent on 26 March 2015, implemented another Graham recommendation, creating a reserve power for the Secretary of State to legislate if necessary in respect of pre-packs. Subject to a sunset provision, this reserve power expired at the end of May 2020, but the Corporate Insolvency and Governance Act 2020 has revived the power until June 2021. The SBEEA 2015 also introduced other measures to modernise various parts of the insolvency framework by removing unnecessary costs and regulatory burdens.

On 12 December 2017, the Insolvency Service announced that it would undertake an assessment of the impact of voluntary industry measures in respect of pre-packaged administration sales to connected parties. The findings of this review to help to inform a decision on whether further regulation is needed.

On 8 October 2020, the Insolvency Service published its report, “Corporate report: Pre-pack sales in administration report”. It notes that, while there had been some improvements to the marketing of pre-packs, there was low use of the pre-pack pool and continued concern around transactions under market value. On the same day as the publication of the report, the Government published draft regulations intended to apply
to all pre-pack administration sales to a “connected” purchaser. Following a consultation, final regulations were laid before Parliament on 27 February 2021 and are due to come into force on 30 April 2021.

This briefing paper looks in detail at how pre-pack administrations work in practice under revised SIP 16; the “pros and cons” of the procedure; the recommendations of the Graham Review; and provides a summary of the measures introduced by the SBEEA 2015. It goes on to consider the Insolvency Service 2020 report and the new regulations on sales to “connected” purchasers. This briefing paper applies to England, Wales and Scotland.
1. Pre-pack administration

1.1 What is the pre-pack administration procedure?

A pre-packaged administration (a pre-pack) is a planned insolvency procedure in 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 insolvency practitioner as administrator. The sale is then completed on the appointment of the administrator or very shortly afterwards. Pre-packs are a means by which administrators realise the assets of an insolvent company. The proceeds of sale are usually used to repay creditors in order to prevent them from exercising fixed charges, and to protect the company from liquidation.

The purchaser may be new to the company or a competitor, but it is also possible that the purchaser may be the existing management. The directors of a failed company may wish to purchase its assets or business in order to form a new company. (This new company is sometimes referred to as a “phoenix company” or a “newco”). In 2011, the Insolvency Service estimated that 25 per cent of the 2,808 companies that entered administration in 2011 used the pre-pack procedure; and that nearly 80 per cent of pre-pack sales were to connected parties.

Many creditors who are owed money by a failed company are outraged to find that the directors of these companies may suffer little personal loss and are often able to start up a new business in the same field. To a certain extent, this is an inevitable consequence of limited liability. For the purposes of the law, a company is a separate legal entity and if it trades with limited liability its directors and shareholders do not usually retain liability for the company’s debts should it become insolvent. However, there are rules in place designed to prevent an abuse of this privilege of limited liability.

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1 Since 26 May 2015, an administrator may now extend his term in office for up to a year (previously 6 months) by consent, without the need for a court application. This is provided for in section 127 of the Small Business, Enterprise and Employment Act 2015.

2 A “fixed charge” may be define as a charge over a particular asset where the ‘chargee’ controls any dealing or disposal of the asset by the ‘charger’. A fixed charge ranks before a floating charge in the order of repayment on an insolvency (see footnote 11 for a definition of a floating charge).

3 A secured creditor, in relation to a company, means a creditor of the company who holds in respect of his/her debt a security over property of the company. Security means, in relation to England and Wales, any mortgage, charge, lien, or other security.

1.2 What is the difference between a pre-pack and a regular administration?

In a pre-pack administration, all the preparatory work for the sale of a company’s assets/business is carried out in advance of formal administration (and usually before the creditors have been told about the failure of the business). Terms are pre-negotiated with a purchaser before an administrator is appointed and the sale contract is executed by the administrator as soon as appointed.

In a regular administration, the administrator begins managing and trading the business and conducting sales negotiations after being appointed. It follows from this that the regular administration process is usually slower and less predictable. The company can usually continue operating throughout the pre-pack administration process, making it possible to preserve brand integrity and retain customers and key employees.

1.3 Why are pre-packs used?

When a business needs to be rescued there are often worries about maintaining brand value – both for existing creditors and for prospective purchasers trying to restart the business. As a result, the practice of ‘pre-packaging’ the administration process has developed. The insolvency practitioner, the directors and the bank will have obtained valuations, agreed a sale price and drafted contracts before the administration order is made, thereby enabling the business to be sold immediately after the appointment of the administrator.

1.4 Effect of administration on employees

If a company in financial difficulty is put into administration (whether or not pre-packaged), it is possible that the business may carry on trading as a ‘going concern’. If the administrator can find a buyer to take over all or part of the business as a going concern, some jobs may be saved (although there may still be redundancies). Employment contracts may be transferred to the buyer, with the employees’ rights protected under special rules that apply to transfers of undertakings.

In contrast, if a company in financial difficulty is put immediately into liquidation, then all jobs will be lost. The company will no longer exist.
2. How are pre-pack administrations regulated?

Currently, pre-packs are not specifically provided for in insolvency legislation; a company does not need the approval of its unsecured creditors or the permission of the court to initiate a pre-packaged administration procedure. However, an insolvency practitioner is an officer of the court and as such is required by law to ensure that a pre-pack sale provides the best outcome for creditors before recommending this course of action. In addition, administrators are required to adhere to a Statement of Insolvency Practice (SIP 16) a mandatory professional standard (see Box 1 below).

Box 1: Annual report on the operation of SIP 16

In May 2012, the Insolvency Service published its Report on the Operation of SIP 16, 1 January to 31 December 2011 (the most recent report available on the GOV.UK site). According to this report:5

- 32 per cent of cases reviewed during 2011 were not fully compliant with SIP 16 disclosure requirements;
- 29 cases (7 per cent of the sample) were referred to the relevant authorising body for being substantially deficient (cases were reported if they failed to provide enough detail or justification to support the pre-pack process or were not sufficiently timely);6
- some insolvency practitioners are failing to comply with requirements in SIP 16 to provide information on pre-appointment costs and expenses, and to obtain approval for them.7

In supplementary evidence given to the Business, Innovation and Skills (BIS) Select Committee,8 the Insolvency Service gave the following figures on the number and the level of fines that had been levied for SIP 16 non-compliance:

Since January 2010 there have been a total of 6 fines given to insolvency practitioners by their authorising bodies for breaches of SIP 16. The fines ranged from £250 to £2,500 with costs attached ranging from £250 to £2,167. In 26 other cases, the authorising bodies took regulatory action resulting in 5 consent orders without financial penalty and 21 formal warnings. There are 10 SIP16 referrals currently with the authorising bodies for consideration.9

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6 Ibid
7 Ibid
8 Now the Business, Enterprise & Industrial Strategy (BEIS) Select Committee
A pre-pack administration (like any other administration) is under the ultimate control of the court. Once appointed, the administrator is required to act in the best interests of all the creditors.\textsuperscript{10} If an insolvency practitioner is found by the court to have acted improperly, he may be made liable for misfeasance (i.e. performing a legal action in an improper way – a cause of action in the civil courts). If he is judged to have acted improperly by his professional body, he will be subject to that body’s disciplinary proceedings.

In addition, the Insolvency Service has enforcement powers to clamp down on any directors who misuse the administration process to disadvantage creditors or seek to gain benefit for themselves. Directors of insolvent companies, which includes those going through administration, can be disqualified by the court for a period between 2 and 15 years if their conduct in the period leading to the insolvency proceedings is considered to be unfit.

\textsuperscript{10} In practice, the administrator may instruct agents to provide a report as to the likely realisable value of the assets and to advise on the best way in which to maximise value in all the available assets.
3. Pros and cons of pre-pack administrations

The pros and cons of pre-pack administrations is a subject much debated within the Insolvency industry. Commenting on how pre-packs work in practice, the Association of Business Recovery Professionals (known as ‘R3’) has said:

If the conditions are appropriate, a pre-pack can be advantageous for all involved, and can be the best way of extracting value from a dire situation.11

The advantages of a pre-pack administration as a company rescue tool are outlined in Box 2 (below).

Box 2: Potential advantages of a pre-pack

It is argued variously that when undertaken in a professional manner, a pre-pack administration may offer some of the following benefits:

- Since the administration process is pre-negotiated, business operations are not interrupted or detrimentally affected
- Jobs may be saved
- Once the pre-pack sale has been arranged, a purchase contract has been drawn up, and an Insolvency practitioner has been appointed as an administrator, the courts keep the company protected from creditor pressure while the company’s assets are sold
- Pre-packs prevents secured creditors from enforcing a charge against the company’s property or assets – allows the company to avoid receivership and bankruptcy
- Assets of a company in financial difficulty may be sold at a higher price since the insolvency practitioner can negotiate with potential buyers before he/she has been formally appointed as administrator.

The potential disadvantages of a pre-pack administrations are outlined in Box 2 (below).

Box 3: Potential disadvantages of a pre-pack

In recent years, pre-pack administrations have raised the following issues:

- Whether businesses are being sold at under-value, especially where this is to the previous owner or a connected party with no open market valuation
- Possible conflicts of interest for the insolvency practitioner, for instance, where there is close working with the directors or when appointed by the floating charge holder12
- Lack of involvement of unsecured creditors, who are only informed of the deal after it has taken place
- The role of advertising targeted at directors of distressed companies

11 The Association of Business Recovery Professionals (R3), Briefing on pre-packaged sales (pre-packs’), undated, [online] (accessed 9 December 2019)
12 A floating charge is a charge on company property that is constantly changing in value and identity (e.g. stock, book debts and work in progress). A floating charge does not attach to a specific item of property. The holder of a floating charge (e.g. a bank) has no right of possession of the assets covered by the charge until one of the events specified in the charge instrument causes the charge to ‘crystallize’ (i.e. a default on repayments of a loan).
• Giving an unfair market advantage by allowing the new company to leave behind its unwanted debts
• Causing longer-term economic harm by allowing inefficient businesses to carry on trading

The new rules introduced under SIP 16 are intended to answer these criticisms, by providing for greater transparency for creditors in the pre-pack administration process.

In recent years, pre-pack sales have been criticised for their lack of transparency. In a majority of cases, sales were agreed prior to the first notification to creditors, and the sales were often made to connected parties (i.e. the existing management). This meant that by the time the creditors received the first report from the administrator, they were presented with the sale as a done deal, and thus had no opportunity to raise any queries or concerns.

For some creditors, there is a perception that company assets may have been sold at an undervalued price or that ‘goodwill’ may not have been fully valued because of the speed of the sale. The matter is further complicated if the purchaser is the existing management, with concerns raised as to the potential for abuse of the process by directors seeking to purchase assets at an advantageous price and simply avoid payment of creditors.
4. Graham review of pre-pack administrations

4.1 Background

The BIS (now BEIS) Select Committee report on The Insolvency Service was published on 6 February 2013. In respect of pre-pack administrations, the Select Committee concluded that they remain a controversial practice:

80. In May 2009, our predecessor Committee expressed concerns about the lack of transparency, resultant abuse of pre-pack administrations and their link to ‘phoenix companies’. Despite the introduction of Statement of Insolvency Practice Note 16 and additional guidance, pre-pack administrations remain a controversial practice. The Insolvency Service is committed to continue to monitor SIP 16 compliance, but to make this effective, non-compliance needs to be followed through with stronger penalties by way of larger fines and stronger measures of enforcement.

The Committee made the following recommendations:

- BIS and the Insolvency Service to commission research to renew the evidential basis for pre-pack administrations;
- the Insolvency Service to amend its monitoring processes to include feedback to each insolvency practitioner and their regulatory body where SIP 16 reports have been judged to be non-compliant; and
- the criteria by which SIP 16 reports are judged to be published alongside the guidance.

In July 2013, Vince Cable, then Business Secretary, announced the appointment of Teresa Graham CBE to undertake an independent review of pre-pack procedure. This followed a speech he gave on the issue of transparency and trust in business. As part of this review, the University of Wolverhampton was commissioned to carry out research based on a large sample of pre-packs from 2010.

On 16 June 2014, the Graham Review into Pre-pack Administration was published, together with a report on pre-pack empirical research, Characteristic and Outcome Analysis of Pre-pack Administration. The

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14 Ibid
15 Ibid
16 This review of pre-packs was part of a wider Government programme to improve corporate transparency. See Department for Business, Innovation and Skills (BIS), Transparency & Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business – Discussion Paper, July 2013, [online] (accessed 9 December 2019)
18 Pre-pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration – Final Report to the Graham Review, Prepared by Professor Peter Walton and Chris Umfreville with the assistance of Dr Paul Wilson, University of Wolverhampton, April 2014, [online] (accessed 9 December 2019)
Graham Report concluded, “the benefits that pre-packaging brings to the UK’s insolvency framework mean that reform of the process is worthwhile, however, there should be some major improvements to how they are administered”.19

Importantly, the Graham Report proposed voluntary scrutiny of pre-pack deals rather than new legislation.

4.2 Graham recommendations

Following pre-pack sales to “connected” parties, the Graham Report found that creditor pay-outs were often worse, and the new business was less likely to succeed.20 The definition of a “connected” party used in the Graham Report is outlined in Box 4 (below).

Box 4: What is a “connected party” for the purposes of the Graham Report?

Although the term “connected party” is defined in the Insolvency Act 1986 (IA 1986), the Graham Report does not adopt this definition. Instead, a “connected party” is taken to mean:

(a) a director, shadow director or company officer of the insolvent company;
(b) an associate21 of a director, shadow director or company officer of the insolvent company; and
(c) an associate of the insolvent (pursuant to section 249 of the IA 1986) who becomes:
   • a director, shadow director, company officer of the new company;
   • exercises control over the new company as defined in section 435(10) of the IA 1986;22
   • an associate of a director, shadow director or company officer of the new company, and
   • an associate of the new company

The Graham Report made six key recommendations particularly targeted at these kind of pre-pack deals (see Box 5 below).

Commenting on these six recommendations, the Government said that it supported the voluntary approach set out in the Graham report:

Teresa Graham has come up with a set of recommendations which will ensure people get back as much money as possible and make pre-pack deals more transparent. We will be working with business and industry to implement these recommendations in full and we believe it will help restore trust and confidence in pre-

19 Ibid

20 Pre-pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration – Final Report to the Graham Review, prepared by Professor Peter Walton and Chris Umfreville with the assistance of Dr Paul Wilson, University of Wolverhampton, April 2014, [online] (accessed 9 December 2019)

21 An “associate” means any person set out in section 435 of the Insolvency Act 1986 with the exclusion of subsection (4) which relates to employees (who are not directors or shadow directors)

22 For the purposes of determining whether any person or company has control of a company under section 435(10) of the Insolvency Act 1986, sales to secured lenders who hold security for the granting of the loan (with related voting rights) as part of the lender’s normal business activities over one third or more of the shares in both the insolvent company and the new company are not included
pack deals. We will monitor progress loosely and will take the power to legislate if necessary.  

Box 5: The Graham Report’s six recommendations:

1. Create a pre-pack pool of experienced business people where, on a voluntary basis, details of a proposed sale to a ‘connected party’ could be disclosed to an independent person prior to the sale taking place, the aim being to increase transparency and give greater confidence to creditors that the deal has undergone independent scrutiny.

2. Request connected parties to complete a ‘viability review’ for the new company, stating how the company will survive for at least the next 12 months. A short narrative will also be provided, detailing what the new company will do differently from the old company in order that the business does not fail again. According to the Graham report, a new company in a connected pre-pack is more likely to fail than a new company unconnected with those controlling the old company. Empirical evidence shows that there is a clear link to future failure in connected party cases.

3. The Joint Insolvency Committee to consider, at the earliest opportunity, a redrafted SIP 16 (found in Annex A of the Graham report). It is proposed that the documents required by the preceding two recommendations (i.e. a report by a pre-pack pool member and a viability review by a ‘connected party’) be sent with the redrafted SIP 16 statement.

4. All marketing of pre-pack businesses to comply with six ‘good marketing’ principles (stated in the report) in order to maximise sale proceeds and that any deviation from these principles be brought to creditors’ attention.

5. SIP 16 to be amended to require valuations to be carried out by a valuer who holds professional indemnity insurance (‘PII’), to increase confidence that the sale is for a fair price.

6. The Insolvency Service to withdraw from monitoring SIP 16 statements. Monitoring to be picked-up instead by the recognised professional bodies (RPBs), as they have the right level of practical experience to further improve compliance rates.

The Graham Report also suggested that the Government should consider taking a reserve legislative power, in order that it could act should the measures outlined above fail to have the desired impact or are not adopted by the market. It recommended that any such reserve power should be time-limited by way of a “sunset clause”.

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24 Pre-pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration – Final Report to the Graham Review, Prepared by Professor Peter Walton and Chris Umfreville with the assistance of Dr Paul Wilson, University of Wolverhampton, April 2014, [online] (accessed 9 December 2019)

5. **Pre-packs: introduction of voluntary measures**

5.1 **Compliance with the latest Statement of Insolvency Practice 16 (SIP 16)**

Since the 1 November 2015, insolvency practitioners have been required to comply with the latest Statement of Insolvency Practice (SIP 16) in connection with pre-pack administrations. The main changes to SIP 16 have been in the area of marketing (see **Box 6** below).

**Box 6: Insolvency Practice 16 (SIP 16)**

SIP 16 sets out the “marketing essentials” these essentials include:

- **Broadcast** – the business must be marketed as widely as possible.
- **Justification of the strategy** – explain the marketing and media strategy.
- **Independence** – ensure that they are satisfied as to the adequacy and independence of the strategy adopted in the marketing process, particularly important where marketing is taking place before the appointment takes effect.
- **Publicise rather than just publishing** – marketing should be over an appropriate length of time.
- **Connectivity** – include the use of online media alongside other marketing by default.
- **Comply or explain** – particularly where the sale is to a connected party with high levels of interest, an explanation needs to be given as to how the marketing strategy achieved the best result for creditors as a whole in all the circumstances.

Taken together, the administrator is required to carry out more transparent marketing of the business prior to the sale.

5.2 **Creation of the “Pre-Pack Pool”**

One of the key recommendations of the Graham report was that a pool of independent people with expertise in business be set up in order to assess and give an opinion upon a proposed pre-pack sale to a “connected person”. This recommendation was adopted, and a **Pre-Pack Pool** came into force on 2 November 2015.

Insolvency Practitioners now need to make connected party purchasers aware of this new Pre-Pack Pool, which operates exclusively online (see **Box 7**). It is not compulsory to use this Pool, but it is considered best practice. It helps ensure transparency for creditors.
Pre-pack administrations

Box 7: The new Pre-Pack Pool

Since 2 November 2015, if a “connected party” wishes to purchase a business that is about to go into administration, then it is recommended that they approach the Pre-Pack Pool, who will independently review the proposed deal prior to it being completed. Applications to the Pre-Pack Pool are submitted via an on-line portal (there is a fee).

Such a recommendation applies only to purchasers who are deemed to be a ‘connected party’. A “connected party” can be a director, shadow director or owner of an insolvent company, or an associate of these parties who then becomes the director, shadow director or owner of the new company.26

The application is considered by one Pre-Pack Pool reviewer, who can give one of three outcomes (usually within 48 hours, so to minimise any disruption):

- the pre-pack purchase is not unreasonable; or
- the pre-pack purchase is not unreasonable, but there are minor limitations in the evidence provided; or
- the case for pre-pack has not been made out

A copy of the reviewer’s opinion is attached to the administrator’s SIP 16 report, which is then sent to creditors. A pre-pack deal can still go ahead, even if a negative statement is received from the pool of experts. However, the administrator would need to set out the reasons for doing so in the SIP 16 report to creditors.

It is important to note that referral to the Pre-Pack Pool by a connected purchaser is only voluntary. However, the administrator’s SIP 16 report to creditors will be expected to disclose the reasons why the connected party decided not to approach the pool for sanction.

Obviously, the main aim of this voluntary scrutiny is to create confidence and transparency in a proposed deal for the benefit of the creditors. The purchaser may also provide a voluntary viability review statement.

This reform has also been reinforced by a revised (SIP) 16 which strengthens the requirements for marketing and independent valuation in pre-pack administration deals.

5.3 Viability statement

A “connected party” wishing to make a pre-pack purchase can draw up a viability statement essentially setting out how the purchasing entity (i.e. the business) will survive for at least the next 12 months, it is proposed that the statement should outline how things will be done differently. Any viability statement should be attached to the SIP 16 Statement made by the administrator. If the statement is requested but not supplied creditors should be made aware of this in the SIP 16 Statement.

The aim of a viability statement is to create confidence and transparency in a proposed deal for the benefit of the creditors. However, it is important to note that submission of a viability statement for connected purchasers is only voluntary.

26 A connected party in this context only, does not include lenders with security by way of voting rights with more than one third of the shares of both the old company and the new company.

As outlined in the previous section, new voluntary industry measures were introduced in November 2015 and arose from the recommendations of the Graham Review. In addition, new insolvency measures were included in the Small Business, Enterprise and Employment Act 2015 (SBEEA 2015), which received Royal Assent on 26 March 2015, and must be taken into account by restructuring and insolvency practitioners. Specifically, Part 10 of the Act includes several measures to amend various parts of the current insolvency framework and modernise insolvency law by removing unnecessary costs and regulatory burdens.

According to the Government, an important aim of the SBEEA 2015 is to ensure that the UK continues to be a trusted and fair place to do business, to create opportunities for small businesses to innovate and compete.27 Further detailed information is set out below.

6.1 New reserve power for Secretary of State

On the basis that the voluntary measures arising from the Graham Report may prove unsuccessful, the SBEEA 2015 inserted into the IA 1986 a reserve power for the Secretary of State to make regulations in the future to either prohibit administration sales to connected parties or to impose conditions or requirements to allow a connected party administration sale to proceed (including via a pre-pack).28 This power to legislate was subject to a sunset provision that expired at the end of May 2020 (without the power being used). However, the Corporate Insolvency and Governance Act 2020 has now revived the power until June 2021.29

Effectively, this reserve power leaves open the potential for more stringent reforms to be introduced by the Government.30

6.2 Administrators’ ability to bring wrongful and fraudulent trading claims

Previously, claims under the IA 1986 for wrongful trading and fraudulent trading were only available to liquidators, not to administrators. In practice, this meant that a company in administration could move directly to dissolution (without any intervening liquidation) without such claims having been considered by an Insolvency

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28 Section 129(4) of the Small Business, Enterprise and Employment Act 2015
29 The Corporate Insolvency and Governance Act 2020 introduced measures to help businesses survive the pressures of the Covid-19 crisis
30 The Insolvency Service is an executive agency of the Department for Business Energy, and Industrial Strategy (formerly BIS)
Practitioner. Alternatively, in order to pursue a wrongful or fraudulent trading claim, the administrator would first have to put the company into liquidation.

The SBEEA 2015 has changed the situation. Specifically, the Act inserts new sections into the IA 1986, to allow an administrator (as well as a liquidator) to bring claims against directors for fraudulent trading and wrongful trading. These provisions came into force on 1 October 2015.

In effect, it is now possible for an administrator to consider potential avenues of recovery during the administration process, rather than delay any investigation until such time as the company moves from administration into liquidation (which may not occur). This should increase the potential for more claims to be brought, and more quickly, for the benefit of the creditors.

Under the SBEEA 2015, administrators and liquidators can also assign causes of action to third parties. Further details are set out below.

**6.3 Administrator’s right to assign wrongful and fraudulent trading claims**

Prior to the SBEEA 2015, administrators and liquidators could only assign causes of action which vest in the company (such as misfeasance claims) but not actions which vest in the office-holder personally. The situation has now been changed by provisions of the SBEEA 2015, which came into force on 1 October 2015.

Specifically, the Act inserts new sections into the IA 1986, which allows liquidators and administrators to assign the following rights of action to third parties:

- fraudulent trading
- wrongful trading
- transactions at an undervalue
- preference transactions; and
- extortionate credit transactions

In addition to conferring the ability to assign such claims, the SBEEA 2015 inserts a new section 176ZB into the IA 1986. New section 176ZB

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31 Sections 117 to 119 of the Small Business, Enterprise and Employment act 2015
32 New sections 246ZA and 246ZB to be inserted into the Insolvency Act 1986 by the Small Business, Enterprise and Employment act 2015. The wording of the new clauses of action mirror the claims available to liquidators under sections 213 and 214 of the Insolvency Act 1986
34 New section 246ZD of the Insolvency Act 1986
35 Section 213 of the Insolvency Act 1986
36 Section 214 of the Insolvency Act 1986
37 Section 238 of the Insolvency Act 1986
38 Section 239 of the Insolvency Act 1986
39 Section 244 of the Insolvency Act 1986
specifically provides that any proceeds recovered from any of the above
listed claims (or recoveries made pursuant to an assignment of such
claims) will not be treated as part of the company’s net property for
distribution to the holders of any floating charge created by the
company.  

Litigation is expensive and funding options are sometimes limited. It is
hoped that the ability to assign such claims will ensure that fewer
actions are hindered due to lack of funding which in turn will lead to
more certainty and a quicker return to creditors.

Taken together, all these amendments should provide increased
flexibility for officeholders to act for the benefit of unsecured creditors.

6.4 Administrator’s fees

The Insolvency (Amendment) Rules 2015 came into force on 1 October
2015. They amended the 1986 Insolvency Rules to introduce a new
approach to the approval and payment of insolvency office holders’ fees
and disbursements.

Administrators, liquidators and trustees in bankruptcy are now obliged
to provide fee estimates to creditors, giving details of the likely
remuneration they will charge, and any expenses likely to be incurred in
the case. These estimates must be provided before the basis of the
officeholder’s remuneration is determined. The approval of the fee
estimate will then effectively cap remuneration at that level, unless
further approval is sought.

6.5 Changes to creditors’ meetings

Sections 122 and 123 of the SBEEA 2015 (which came into force on 6
April 2017) have amended the IA 1986 by inserting new sections 246ZE
to 246ZG and 376ZC to 379ZA. These amendments mark a significant
change in how decisions of creditors will be taken in all types of
insolvency proceedings. These sections together with Part 15 of the
new Insolvency (England and Wales) Rules 2016 (“the IR 2016”)
(which also came into force on 6 April 2017) flesh out an entirely new

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40 A floating charge is a charge on company property that is constantly changing in
value and identity (e.g. stock, book debts and work in progress). A floating charge
does not attach to a specific item of property. The holder of a floating charge (e.g. a
bank) has no right of possession of the assets covered by the charge until one of the
events specified in the charge instrument causes the charge to ‘crystallise’ (i.e. a
default on repayments of a loan).

41 By way of background information, Part 2 of the Legal Aid, Sentencing
and Punishment of Offenders (LASPO) Act 2012 reformed the operation of “no win, no
fee” conditional fee agreements (CFAs). These reforms came into effect generally in
April 2013 but were delayed in respect of insolvency proceedings. However, this
exemption ended on 1 April 2016. Since this date, officeholders have been unable to
recover “no win, no fee” CFA success fees and after-the-event (ATE) insurance
premiums from losing defendants. (See HL Deb. 17 December 2015 c410WS).

42 SI 2016/1024

43 Although an estimate of expenses is required, there is no requirement for the expenses
to be approved

44 It should be noted that this obligation does not apply to supervisors of Individual
Voluntary Arrangements (IVAs), Company Voluntary Arrangements (CVAs) or to a
liquidator in a Members’ Voluntary Liquidation (MVL)
decision making regime. Key features of this new regime are outlined in Box 8 (below).

**Box 8: Changes to creditors’ meetings: new rules specifying alternative forms of decision making:**

**Restrictions on use of physical meetings**

Whereas the **IA1986** placed heavy reliance on physical meetings, under the new regime an officeholder cannot summon physical meeting of creditors unless requested by to do so by either 10% of the creditors in value, 10% of the total number of creditors or 10 individual creditors.\[46\]

**New procedure for deemed consent**

New sections 246ZF and 379ZB of the **IA 1986** provide that where an officeholder writes to the creditors with a proposal, and does not receive objections from 10% of creditors in value, the proposal is deemed to be approved. This procedure is available unless the court or the insolvency legislation requires the use of a “creditors’ decision-making procedure”.

**Alternative creditors’ decision-making procedures**

**Rule 15.3** of the IR 2016 defines the following procedures that may be adopted as an alternative to deemed consent:

- correspondence
- electronic voting\[47\]
- virtual meeting\[48\]
- physical meetings (subject to the aforementioned restriction)\[49\]
- and any other decision-making procedure which enables all creditors who are entitled to participate in the making of decisions to participate equally.

As outlined in Box 8, physical meetings are prohibited except where creditors request them. Instead, insolvency practitioners (in both corporate and individual insolvencies) can use the “deemed consent procedure” when asking creditors to decide about a matter. In a nutshell, the insolvency practitioner will provide a notice with details of the proposed decision, and an explanation of how to object. If less than 10 per cent in value of creditors object to the proposed decision, it will be deemed to have been approved.\[50\] Decisions can be made in this way unless the **IA1986** or the court requires that a “qualifying decision procedure” is to be followed. These procedures are set out in **Rule 15.3** of the IR 2016 and involve virtual meetings, electronic voting or meetings by correspondence.

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\[46\] Section 246ZE and 379ZA, Insolvency Act 1986
\[47\] Rules 15.2 to 15.4 of the Insolvency Rules 1986
\[48\] Rules 15.2 and 15.5 of the Insolvency Rules 2016
\[49\] Rule 15.2 and 15.6 of the Insolvency Rules 2016
\[50\] Sections 246ZE to section 246ZG of the Small Business, Enterprise and Employment Act 2015 for corporate matters, and sections 379ZA to 379ZC of the Act for individual insolvencies
Importantly, creditors still have the right to request that the insolvency practitioner summon a physical meeting under Rule 15.6 of the IR 2016 (see Box 9 below).

Box 9: Creditors right to request a meeting

- The new rules provide that creditors representing at least 10% in number or value or 10 creditors in total (i.e. any one of these criteria) can require a meeting to be held.
- In effect, only a relatively small number of creditors can request a meeting in most cases.
- It is important to note that Company Voluntary Arrangement (CVA) and Individual Voluntary Arrangement (IVA) meetings will continue to be held in all cases. These meetings are held to decide whether to approve the proposals put forward by a company (CVA) or individual (IVA) for a compromise arrangement with their creditors; the outcomes are binding on all creditors.

Creditors are also able to opt out of being sent paperwork regarding insolvencies. The aim being to reduce unnecessary costs associated with meetings being held where, for example, no one turns up, as well as large amounts of paperwork being printed and sent that simply isn’t read.

It is hoped that these changes will reduce the cost and delay incurred by arranging creditor meetings. However, some commentators have expressed concern that the views of creditors may not be adequately addressed without actual meetings taking place, in particular in relation to so-called “Paragraph 51 meetings” when creditors meet immediately after the company is placed in administration and discuss and vote on the administrator’s proposals. Some commentators are concerned that fewer of these meetings will result in less creditor engagement.

The onus is very much on the creditors: they can still have meetings and paperwork if they want.
7. Assessment of the impact of the voluntary measures

7.1 Insolvency Service review: December 2017

As outlined above, as a result of the Graham Review, voluntary industry measures were introduced in November 2015 to improve the transparency of connected party pre-pack sales in administration. In addition to these voluntary reforms, the SBEEA 2015 inserts into the IA 1986 a power for the Government to regulate or ban sales in administration to connected persons (including via a pre-pack). This power to legislate was subject to a sunset provision that expired at the end of May 2020 (without being used). However, the Corporate Insolvency and Governance Act 2020 has revived the power until June 2021.\(^{51}\)

On 12 December 2017, the Insolvency Service announced that it would undertake an assessment of the impact of the voluntary measures to help to inform a decision on whether further regulation is needed. As part of this assessment, the Insolvency Service contacted a variety of interested parties to seek their views.\(^{52}\) For instance, in May 2018, R3 (the insolvency and restructuring trade body) published its Evaluation of Industry Measures to Improve Transparency of Connected Party Pre-pack Administration Sales Submission.

7.2 Final report & draft regulations: October 2020

The Insolvency Service published its final report, “Corporate report: Pre-pack sales in administration report”, on 8 October 2020. It concluded that the Government does not intend to ban pre-packaged administration sales to connected parties altogether, but concerns remain around pre-pack administrations to connected parties. It notes that, while there had been some improvements to the marketing of pre-packs, there was low use of the pre-pack pool and continued concern around transactions under market value. On the same day as the publication of the report, the Government published draft regulations which would apply to all pre-pack administration sales to a “connected” purchaser, requiring an independent opinion from an evaluator on the sale. The aim was to provide stakeholders with greater assurance that such sales would be appropriate in the circumstances.

For the Government, this regulatory approach is “a good balance between the stated concerns, and not blocking the use of a useful company rescue tool”.\(^{53}\) Lord Callanan, Minister for Climate Change

\(^{51}\) The Corporate Insolvency and Governance Act 2020 introduced measures to help businesses survive the pressures of the Covid-19 crisis.

\(^{52}\) Insolvency Service, An assessment of the impact of the voluntary industry measures introduced in November 2015 is to be undertaken, 12 December 2017, [online] (accessed 9 December 2019).

and Corporate Responsibility, explained the policy rationale for the legislative proposals as follows:

I recognise that pre-pack sales are a valuable part of the insolvency landscape, representing around 29% of all administrations. They can be a useful tool to rescue businesses, saving jobs and preserving value. However, creditors are often unaware of the sale until the transaction has completed and pre-packs can be controversial where the business is sold to a person connected with the insolvent company, for example existing management or family members. Although this may sometimes deliver the best outcome possible in the circumstances.

We have reviewed the effectiveness of the package of voluntary measures introduced in 2015 to improve creditor confidence in pre-pack sales. Despite some improvement in how businesses are marketed, and the provision of more information being made available for creditors, concerns remain about the transparency of pre-pack sales and whether they are always in the best interest of creditors. This is particularly the case where the sale is to a connected person, which represent around half of all pre-pack sales. These issues were highlighted during the recent Parliamentary debates on the Corporate Insolvency and Governance Act.

We need to address these concerns in order to improve confidence in the process and the Government will therefore be bringing forward legislation which places certain conditions on connected person sales in administration. We will also take steps to strengthen professional regulatory standards and improve the quality of the information provided to creditors.

Together, these reforms will improve transparency and creditor confidence in the pre-pack process, contributing to the strength of the UK’s first-class insolvency framework. The measures will promote viable business rescue while balancing the rights of those affected by failure and will contribute to leading the country’s economic recovery from Covid-19.54

Insolvency practitioners and other stakeholders had until the 5 November 2020 to comment on the draft regulations.

7.3 Final regulations

On 24 February 2021, The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 were laid before Parliament. These regulations are due to come into force on 30 April 2021, following approval by each House of Parliament.

The explanatory memorandum which accompanies the new regulations, explains the changes made to the draft regulations following consultation in October 2020:

Comments received by stakeholders (including the Recognised Professional Bodies, R3, PPF) were centred on the qualification requirements of the evaluator and concerns about disclosure of previous reports obtained by the connected person. This led to alteration and strengthening of the regulations which will ensure they have the desired impact. Changes to the regulations include

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54 Insolvency Service, Corporate report: Pre-pack sales in administration report*, Section 1 – Forward, 8 October 2020, [online] (accessed 21 October 2020)
provisions aimed to disincentivise a person obtaining multiple reports in the hope that one would be favourable and strengthening the requirements for acting as an evaluator by including an obligation to obtain suitable insurance.

The Regulations, if enacted, mean that an administrator cannot execute a pre-pack if all of the following apply:

- The sale (or other form of disposal, including hiring out) is of all or substantially all of the insolvent company’s business or assets.
- It is within the first 8 weeks of an administration.
- The disposal is to one or more persons connected with the company.
- Either the administrator has not obtained the approval of creditors or the purchaser has not obtained and provided a “qualifying report” of an evaluator.

In effect, where an administrator wishes to dispose of all or a substantial part of a company’s assets within the first 8 weeks of the administration to one or more connected persons, the administrator will need to obtain creditor 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 evaluator’s written opinion must be commissioned by the purchaser(s) and should include:

- a statement whether the evaluator is or is not ‘satisfied that the consideration to be provided for the relevant property and the grounds for the substantial disposal are reasonable in the circumstances’;
- the evaluator’s reasons for coming to their opinion;
- the consideration that will be paid; and
- the identity of the connected person and their connection to the company.

Under the draft regulations, an administrator is not bound to accept the evaluator’s opinion. Even where a report states that the case is not made for the disposal, an administrator can still proceed with the sale but must provide a statement setting out their reasons for doing so. However, as an officer of the court, the administrator would need to have good reasons to ignore a wholly negative opinion. New provisions in the Regulations also seek to disincentivise purchasers from obtaining multiple reports in the hope that will be favourable.

The evaluator must be independent and have the requisite knowledge and experience to prepare the written opinion. The evaluator must not be the administrator or one of their associates, nor may they be connected to the company or the connected person themselves.

Evaluators still require no professional qualifications. Evaluators are qualified if they think they are55 and must otherwise simply be independent, solvent, and without any blemishes on their record under the directors’ disqualification or charities regimes. Importantly, the

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55 Regulation 10(a), Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021
Regulations now require that the evaluator obtain professional indemnity insurance. There is no provision or regulation as to what fees evaluators might charge, although such fees would be borne by the purchasers who engage them in any event.

Not requiring qualifications from evaluators has attracted industry scrutiny. There are also concerns that the Regulations still unnecessarily catch disposals that are only brokered and negotiated after the start of the administration, which already face some creditor scrutiny. Until government guidance is published, it is also unclear whether the pre-pack pool will continue in existence to provide an opinion. Non-legislative measures

7.4 Non-legislative measures

In its 2020 report, the Government said that it intends to work with the industry and the Recognised Professional Bodies (RPBs), who regulate insolvency practitioners, to prepare guidance to accompany the regulations and to ensure SIP16 (Statement of Insolvency Practice) is compatible with the legislation. In addition, the Government said that it intends to strengthen the existing regulatory requirements in SIP 16 to improve the quality of information provided to creditors. It said:

We will also look to strengthen the existing regulatory requirements in SIP 16 to improve the quality of information provided to creditors. We will in particular work with the regulators to ensure:

- there is greater adherence to the principles of marketing;
- where no marketing has been undertaken that this is fully explained by the administrator and any explanation probed by the regulator where necessary;
- there is a continued increase in compliance with the reporting requirements under SIP16; and
- it is understood why viability reports are not being completed and how this could be improved.56

Importantly, the Government said that should these non-legislative measures be unsuccessful in improving regulatory compliance, the quality of the information provided to creditors and the transparency of pre-pack sales in administration, it will consider whether supplementary legislative changes are necessary.57

57 Ibid
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