Changes to law on 'pre-packs' wide of the mark?

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THE term 'pre-pack' is used when a company is put into administration and its business and/or assets immediately sold by the administrator under a sale that was arranged before the administrator was appointed.

The main criticisms of pre-packs centre around a lack of transparency and fairness, whereby unsecured creditors may not be aware of the planned pre-pack sale and so have no opportunity to protect their interests by considering and voting on the pre-pack proposal.

On April 30 2021 new rules on pre-pack sales to connected persons come into force, introduced by the UK Government in response to longstanding criticism surrounding the apparent unfairness to creditors. They attempt to reassure creditors that further safeguards will exist to place barriers to a pre-pack to connected persons, notwithstanding the more debtor-friendly changes introduced over the past year designed to promote a rescue culture throughout the pandemic.

The Administration (Restrictions on Disposal etc to Connected Persons) Regulations 2021 attempt to address these criticisms by introducing a new set of minimum standards that administrators must follow during a pre-pack in order to balance the interests of all involved. An administrator cannot implement a pre-pack if all of the following apply:

- the sale is of all or substantially all of the insolvent company's business or assets
- it is within the first eight weeks of an administration
- the disposal is to one or more persons connected with the company (as defined in the Insolvency Act 1986)
- either the administrator has not obtained the approval of creditors or the buyer has not obtained and provided a 'qualifying report' of an evaluator

In practice, it would seem unlikely that administrators would wish to obtain the approval of creditors given the time this process might take and so a written report from an evaluator as to the reasonableness of a proposed pre-pack is the more likely approach, and will essentially replace the role of the rarely used, voluntary option, 'pre-pack pool' (a group of independent experts who may consider and provide an opinion on whether a proposed pre-pack is fair and reasonable). The key difference from the current regime is that this will become a compulsory requirement before a pre-pack to a connected person can occur.

There is surprisingly little detail in the draft regulations to govern who the independent evaluator should be and what qualifications they should have. As currently drafted, the evaluator is essentially allowed to self-certify their ability to provide the report on the proposed pre-pack.

Significantly, it should also be noted that if the pre-pack report from the evaluator is not favourable, administrators may still proceed provided they have a favourable opinion from another evaluator and provide a statement justifying their decision.

It is difficult to see what practical difference the regulations are likely to make. Although the pre-pack report will be a newly-introduced mandatory step in the process, the fact that an evaluator's opinion could be unfavourable but ultimately disregarded does not necessarily address the current problem surrounding the seldom used pre-pack pool's inability to block a sale that it finds to be unreasonable.

In addition, the role of evaluator being essentially left to the market rather than regulated by the government casts serious doubt on how effective this new step will be in providing those safeguards for aggrieved creditors.