Pre-pack receiverships: The new game in town

Kevin Prendergast looks at the increased use of Pre-Packs in Ireland and their use in the UK where they’ve become commonplace.

Of course there are other advantages. In comparison with its nearest legislatively based equivalent, i.e. examinership, there is no judicial oversight, and, consequently, no independent consideration as to whether the proposals are in the best interests of the wider body of creditors. There is no transparency. Typically, third parties, employees and other relevant stakeholders know little, or nothing, until the transaction is complete. The purchasing party can cherry-pick those elements of the business that they wish to take forward, and leave the remainder to wither, eventually (presumably) through liquidation.

The three cases above are only a selection of those which have been mentioned in the media. There may be many more pre-pack receiverships taking place outside of the full glare of publicity. The last four years have seen a massive upsurge in receiverships, from 59 in 2008 to 533 in 2011 (the most recent year for which the Companies Registration Office has released figures). There are no figures available for how many of these might be categorised as pre-packs, but anecdotally the numbers are also on the increase.

The UK

In the UK, the use of pre-packs has become commonplace in the past few years, albeit typically in the context of administration rather than receivership. Administration is similar to examinership here but with much less formality and oversight attached to the process. For example, if a financial institution has the right to appoint an administrator under the terms of its loan agreement, it can do so without a hearing but, rather, by merely faxing the relevant Court office. The primary purpose of administration is company rescue, unless a better return for creditors can be achieved by continued trading accompanied by a partial or whole company sale as a going concern. Only failing these can the administrator move to secure funds to make a distribution.

In 2011 the UK Insolvency Service estimated that some 25% of the 2,908 companies that entered administration that year used the pre-pack procedure.

The UK has taken some tentative steps to regulate how pre-packs are carried out, most notably by the introduction of a Statement of Insolvency Practice, SIP 16 (issued jointly by the recognised professional bodies and the UK Insolvency Service). This brief document highlights some of the key tenets that Insolvency Practitioners (“IP”) should apply when considering whether to accept such engagements and, thereafter, in conducting such engagements. These include the importance of:

- being clear as to the nature and extent of the IP’s role and relationship with the directors in the pre-approntment period. Specifically, where appointed to advise the company, IPs should make clear that their role is to advise the company and not the directors as regards their personal positions;
- the duties and obligations that IPs owe to the creditors in the pre-approntment period. In particular, they should be mindful of the potential liability which may attach to any person who is party to a decision that causes a company to incur credit in circumstances where there is no good reason to believe that it will be repaid;
- proper disclosure to creditors as to why a pre-pack was executed.

Even with this standard in place, the UK Government is now reviewing the operation of pre-packs following concerns raised, in particular, by creditors, who very often only find out a pre-pack has taken place when they try and recover a debt.

All this, however, is a step ahead of where things currently stand in this jurisdiction, where the SIP does not apply.
Among the more contentious aspects of pre-packs are those where, after the receivership has taken place, it emerges the new owners are effectively the same people who owned the business previously. This is a particular issue in the context of the UK review, where it is estimated that, in some 80% of cases, sales are to connected parties.

**Irish Law**

Under Irish law this brings about some specific issues. For example, a substantial property transaction between a company and one of its directors needs formal sanction from the company’s membership under section 29 of the Companies Act 1990. Of course, if the directors are also substantial, or the sole shareholders of the company this may not present an issue but it is, nevertheless, a requirement that must be complied with. Another important consideration is the prohibition on Receivers from selling significant assets to Officers (and connected persons) of the company without giving the creditors 14 days’ notice. The purpose of these statutory provisions is clearly to protect the company’s members and creditors respectively. In addition, anyone involved in a pre-pack should be conscious of the risks associated with being involved in any transaction(s) entered into by a company for the purpose of intentionally defrauding creditors.

Another important consideration that must be borne in mind is the risk that the organisation appointing the Receiver, through its actions, might be found to have acted as a Shadow Director of the company, thereby subjecting itself to many of the responsibilities and obligations attaching to formally appointed Directors.

The Minister for Jobs, Enterprise and Innovation has indicated recently that he has asked his Departmental officials to review the issue of pre-packs, in particular in the light of the media coverage associated with the Thomas Crosbie Holdings restructuring, elements of which are still playing out before the Courts. No doubt the UK experience will feed into that review, as will the availability of other forms of restructuring, for example the more streamlined examinership proposed in the new Companies Bill for small and medium sized companies. The uptake of that proposal may ultimately be predicated on the availability of an alternative restructuring option that currently operates with no oversight by the Courts, no right of review by the creditors, and no transparency for other stakeholders.

1. Source: Companies Registration Office Annual Report 2011
3. Review announced by the UK Insolvency Service on 12 March 2013
5. Section 316A(3), Companies Act 1963
6. Sunday Independent, 28 April 2013