

Insolvency Practitioner Policy Section
Insolvency Service
3rd Floor, Zone B
21 Bloomsbury Street
London WC1B 3QW

29 June 2011

Dear Sir

Pre-packaged administration sales

I am writing to comment on the proposed changes to The Insolvency Rules 1986, as set out in the draft Statutory Instrument recently published for consultation entitled The Insolvency (Amendment) (No 2) Rules 2011.

In March last year the British Printing Industries Federation (BPIF) responded to the *Consultation/Call for evidence on improving the transparency of, and confidence in, pre-packaged sales in administration*. We stated then that we did not consider that the current framework governing the operation of pre-pack sales in administration provided a sufficient level of confidence that pre-packs were only being used in appropriate circumstances and with an appropriate degree of transparency. We remain concerned that these controversial business rescue arrangements enable the debts of previous owners to be written off, and as such they have rightly attracted fierce and justifiable criticism from creditors and competitors alike. Creditors are aggrieved because they have lost money owed to them, and competitors because they are now faced with a rival that now has an unfair trading advantage. In an over-capacity industry such as printing, which is dominated by small companies, the incidence of pre-pack administrations is disproportionately high and the damage caused to both creditors and competitors alike has been very significant.

We are therefore pleased that action is now being taken to introduce additional controls on pre-pack administrations and that these will also extend to liquidations. We also support the specific measures set out in the draft Statutory Instrument: they are in our view the minimum necessary to ensure the restoration of public confidence in pre-packs. We would urge that the proposed measures should not be watered down in order to accommodate concerns that may be put forward by those with vested interests in retaining the status quo as a consequence of the fee income they currently earn from the sale of failed businesses.

We support the proposal that where a pre-arranged sale has been, or is in the process of being negotiated at the time of appointment, a record should be made in the office-holder's 'consent to act' document that the prospective sale price represents, in their view, the best value for creditors. However the wording "will achieve a better result for the company's creditors as a whole than anything else" is open to a wide range of interpretation. We believe that that administrator should be required to state the reasoning that has led them to reach this conclusion, the steps they have taken to investigate other options, and the rationale for discounting any other options that may have emerged. In particular there must be a requirement to test the market for prospective buyers rather than merely concluding arbitrarily

that no one other than a connected party (usually the in-house management team) would be interested in purchasing the business.

This should be done by open marketing, to avoid the risk that limited marketing only might take place to a tame list of prospects that may not necessarily be particularly likely to show much interest. It is also necessary in order to eliminate any suspicions that might otherwise arise of possible collusion between the administrator and the connected party purchasing the company: this is particularly important if the administrator has had previous involvement with the company's directors in any business recovery or restructuring actions taken earlier in an effort to try avoid administration.

While some might argue that open marketing could further destroy value in a distressed business, particularly where competitors are hungry for new contracts and customers may be concerned about continuity of supply, we would argue that this is only likely to be the case in businesses that have failed as a consequence of having been poorly run by the existing management, who may well see pre-packing as an easy route to dumping accumulated debts. In an over-capacity sector such as printing, the fact that unviable businesses can be resurrected from failure through pre-packing, thereby dumping debts and gaining unfair competitive advantage over their rivals, creates market distortion. Pre-packs militate against necessary industry consolidation that would otherwise improve the trading position and future prospects of other companies, who have managed to remain in business by operating efficiently and providing a quality service while continuing to maintain their payment obligations to their suppliers. Any jobs preserved as a result of allowing a failed business to be preserved through pre-packing are often more than outweighed by those lost in competitor companies, whose trading position is then undermined by the unfair competitive advantage achieved by the pre-packed company. This is accentuated in those instances, by no means unknown in the printing industry, where the pre-packed company has gone on to fail again after a relatively short period of time.

In such circumstances, the in-house management are therefore probably the last people qualified to be running the new company. On the contrary, other companies would benefit from being able to absorb the trade previously undertaken by the failed business should the pre-pack sale not be undertaken. Since these businesses are not distressed, the economic value preserved in the trade as a result would be better preserved, offering greater protection for employees, customers and suppliers. While we acknowledge that in tough trading conditions some of the pre-pack's competitors may also be struggling, one thing that could bring them down as well is the resurrection of a failed business that is now able to compete against them more advantageously as the result of freeing itself of its previous debts. The fact that the number of prepack sales to in-house managements (sometimes known as 'same director prepacks') might decline as a consequence of open marketing should not therefore be seen as detrimental to the UK's economic interests.

Of course well-managed businesses can fail too, often as the result of adverse circumstances that are outside the control of the management team, such as unforeseeable bad debts or unexpected customer collapse for example. But in these circumstances we would argue that the underlying strength of these companies will usually make them an attractive proposition to prospective purchasers, meaning that in these cases the residual value of the business is more likely to *increase* as a result of open marketing.

We also support the proposal to require administrators and liquidators to give three days' notice to all known creditors of the terms of any proposed sale, where the office-holder intends to sell a significant proportion of the assets of a company or assets which are necessary to the continuance of the business (or a significant part of the business) of the company to a connected party where there has been no open marketing of the assets. However we believe that notice should be given in *all* circumstances, and as stated above we would also maintain that there should be a requirement to openly market the business in all cases, using suitable communications media that are well-known and well-visited in the industry concerned, such as the publications and websites of trade associations and trade magazines.

We also support the proposal that where a significant proportion of the assets of a company, or assets which are necessary to the continuance of the business (or a significant part of the business) of the company have been sold by the office-holder to a party (whether connected or not) before the administrator's proposals or the liquidator's first progress report have been issued, there should a requirement for a detailed explanation and justification for the sale (analogous to that currently required by SIP 16) in the administrator's proposals, to be provided to creditors. However given that competitors as well as creditors are affected by pre-packs, we believe that these reports should be made publicly available, in order to offer wider transparency among the business community and general public as a whole.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Andrew Brown', written in a cursive style.

Andrew Brown
Public Affairs Advisor

Tel 07801 981 306
Email andrew.brown@bpif.org.uk