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The Rise of Pre-Packs as a Restructuring Tool: Theory, Evidence and Policy

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Abstract

The use of pre-packs as a restructuring tool has been traditionally popular in the United Kingdom and the United States. In recent years, however, several jurisdictions around the world, including Singapore, India, Spain, the Netherlands, and the Philippines have promoted the use of pre-packs. By shortening the length of insolvency proceedings, pre-packs have the ability to reduce the costs of financial distress, and especially those associated with the loss of reputation, employees, suppliers and goodwill. Thus, pre-packs can help maximise the value of the firm for the benefit of debtors, creditors, and society as a whole. However, the conflict of interests, lack of transparency and various forms of opportunistic behaviour that could potentially arise from the use of pre-packs have raised some concerns about the desirability of this restructuring tool. This article analyses the concept and types of pre-packs generally found around the world, as well as their similarities and international divergences. It will also review the empirical evidence on pre-packs with the purpose of getting a better understanding of the actual features, risks and outcomes of this restructuring tool. It will conclude by discussing whether countries should promote the use of pre-packs and, if so, how this mechanism can be adopted to serve as an efficient restructuring tool while providing effective protection to creditors.

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1. Introduction

The use of pre-packs as a restructuring tool has become increasingly popular in recent years. In the United Kingdom, many going concern sales have taken place through pre-packaged administrations.[1] In the United States, pre-packaged reorganisation procedures have enabled many financially distressed firms to quickly emerge from bankruptcy.[2] In 2017, Singapore introduced a pre-packaged scheme of arrangement that provides companies with an expeditious and efficient restructuring tool, as shown by various cases that have successfully completed a pre-pack.[3] In the past years, various jurisdictions around the world have decided to regulate or at least promote the use of pre-packs. Among others, India has introduced a pre-packaged insolvency resolution process for micro, small and medium-sized enterprises ("MSMEs"),[4] and various courts in the Netherlands,[5] and more recently Spain,[6] have also allowed debtors to conduct a pre-pack.

By shortening the length of insolvency proceedings, pre-packs can help to reduce the costs of financial distress, particularly those associated with the loss of reputation, employees, suppliers and goodwill. Thus, pre-packs can help to maximise the value of the firm for the benefit of debtors, creditors, and society as a whole. However, the conflict of interests, lack of transparency and various forms of opportunistic behaviour that could arise from some pre-packs have raised some concerns about the desirability of this mechanism as a restructuring tool.

Section 2 analyses the concept and types of pre-packs generally found around the world, as well as their similarities and divergences. Section 3 provides a theoretical assessment of the advantages and risks of pre-packs as a restructuring tool. Sections

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[1] For a general overview of the importance and features of pre-packs in the United Kingdom, see Sandra Frisby, 'A Preliminary Analysis of Pre-packaged Administrations: Report to The Association of Business Recovery Professionals' (R3, London, August 2007) (available at https://www.iiiglobal.org/sites/default/files/sandrafrisbyprelim.pdf); John Armour, 'The Rise of the "Pre-Pack": Corporate Restructuring in the UK and proposals for reform' in RP Austin and Fady JG Aoun, *Restructuring Companies in Troubled Times: Director and Creditor Perspectives* (Sydney University Press, 2012); Peter Walton, Chris Umfreville, and Paul Wilson, *Pre-pack Empirical Research: Characteristic and Outcome Analysis of Pre-pack administration* (University of Wolverhampton, April 2014) (available at http://data.parliament.uk/DepositedPapers/Files/DEP2014-0860/Report_to_the_Graham_review_by_the_Univers....pdf).

[2] For a comprehensive database on the number of pre-packaged reorganisations filed from 1980 to 2021, see UCLA-LoPucki Bankruptcy Research Database, 'Prenegotiation by year—Study summary' <https://lopucki.law.ucla.edu/design_a_study.php?OutputVariable=Prepackaged> accessed 5 September 2021.

[3] For an analysis of the first pre-pack completed in Singapore, see Debby Lim, 'Singapore's First "Pre-Packaged" Scheme of Arrangement' (Singapore Global Restructuring Initiative, 5 February 2021) (available at https://ccla.smu.edu.sg/sgri/blog/2021/02/06/singapores-first-pre-packaged-scheme-arrangement). For other successful cases of pre-packs, see note 56.

[4] The Insolvency and Bankruptcy Code, 2016 (No. 31 of 2016), Chapter III-A.

[5] See Pauline Springorum and Rianne van Pelt, 'Can the pre-pack pack its bags in the Netherlands?' (Leiden Law Blog, 19 November 2019) (available at https://www.leidenlawblog.nl/articles/can-the-pre-pack-pack-its-bags-in-the-netherlands).

[6] See Adrian Thery, Borja Garcia-Alaman, Juan Verdugo and Juan Maria Jimenez Moreno, 'Spanish insolvency pre-pack new feature: appointment of a silent administrator' (Lexology, 26 January 2021) <https://www.lexology.com/library/detail.aspx?g=10ccfff0-16a3-40d3-9bc0-a27cfe4dac0e> accessed 19 August 2021.

4 and 5 review the empirical literature on pre-packs with the purpose of getting a better understanding of the actual features, risks and outcomes of this restructuring tool. Section 6 discusses whether countries should adopt or improve their regulatory framework for pre-packs and, if so, how they can do so. Section 7 concludes.

2. Concept and types of pre-packs: A global perspective

2.1. Introduction

A pre-pack generally refers to a type of *hybrid procedure* combining the advantages of informal workouts (especially in terms of flexibility, speed, confidentiality, and low costs and stigma) with those existing in formal insolvency proceedings.[7] However, while the term "pre-pack" is used in many jurisdictions, the structure and regulation of pre-packs differ significantly around the world, and the concept of a pre-pack should also be distinguished from other similar terms such as pre-arranged (or pre-negotiated) reorganisations and sales of assets.

2.2. Pre-arranged reorganisations and sales

A pre-arranged reorganisation is a regular reorganisation procedure. However, debtors and creditors exchange information and negotiate the content of a *reorganisation plan* prior to the commencement of a formal reorganisation procedure.[8] Due to the informal agreements and lower asymmetries of information between debtors and creditors, a reorganisation plan can then be concluded more quickly once the debtor initiates an insolvency proceeding. Therefore, the prior negotiations between debtors and creditors can reduce the length and costs of insolvency proceedings. Since a pre-negotiated reorganisation only consists of planning *ex ante* how the actual reorganisation procedure will be conducted, this restructuring strategy can be observed in any jurisdiction with a reorganisation procedure. While a pre-arranged reorganisation usually consists of the pre-negotiated debt restructuring, nothing prevents debtors and potential investors from pre-negotiating a future *sale of assets* in bankruptcy, even if this transaction is ultimately subject to the general rules existing for the sale of assets in reorganisation procedures.

A pre-pack is slightly different from a pre-negotiated reorganisation or asset sale. To understand the concept of pre-packs, it is important to distinguish two primary forms of pre-packs generally found around the world: pre-packaged reorganisations and pre-packaged sales.

2.2. Pre-packs

[7] See Jose M. Garrido, 'Out-of-Court Debt Restructuring' (World Bank Study, 2012) (available at https://openknowledge.worldbank.org/handle/10986/2230), 49.

[8] For the concept of pre-negotiated reorganisations, see Dennis F Dunne, Dennis C O'Donnell and Nelly Almeida, 'Pre-packaged Chapter 11 in the United States: An Overview' (Global Restructuring Review, 11 December 2019) <https://globalrestructuringreview.com/guide/the-art-of-the-pre-pack/edition-1/article/pre-packaged-chapter-11-in-the-united-states-overview> accessed 6 September 2021. See also Garrido (n 7).

2.2.1. Pre-packaged reorganisations

In a *pre-packaged reorganisation*, the debtor formally solicits acceptance of a reorganisation plan prior to the commencement of a reorganisation procedure.[9] Once the necessary majorities of creditors are obtained, the debtor initiates a formal reorganisation procedure requesting the court to quickly confirm the plan.[10] Therefore, the reorganisation proceeding can conclude in a few days.[11] This type of pre-packs has traditionally been found in the United States.[12] It also inspired the pre-negotiated rehabilitation procedure that exists in the Philippines and the pre-packaged scheme of arrangement introduced in Singapore.[13]

Pre-packaged reorganisations have also inspired other accelerated forms of debt restructuring mechanisms such as the *summary reorganisation procedures* existing in several jurisdictions, such as Japan, South Korea, and Spain,[14] as well as the *out-of-court debt restructuring agreement* subject to judicial homologation implemented in many countries around the world, including Argentina, Brazil, Italy, Spain and Uruguay.[15] While both types of debt restructuring procedures have often been

[9] *Ibid*.
[10] *Ibid*.
[11] Prepackage filings were consistently within a range of 50-100 days from filing to emergence, averaging nearly 80 days to emerge. See John Yozzo and Samuel Star, 'For Better or Worse, Prepackaged and Pre-Negotiated Filings Now Account for Most Reorganizations' (2018) 37 (11) *ABI Journal*, 64–67.
[12] *Ibid*.
[13] For an analysis of the pre-negotiated rehabilitation adopted in the Philippines, see Antonio Jose Gerardo T Paz, 'Philippines' in Corporate Restructuring and Insolvency in Asia (ABLI Legal Convergence Series 2020), 570-571. For the origins of the Singapore scheme of arrangement, see Ministry of Law, 'Report of the Committee to Strengthen Singapore as an International Centre for Debt Restructuring' (Ministry of Law, 20 April 2016) (available at https://www.mlaw.gov.sg/files/news/public-consultations/2016/04/Final%20DR%20Report.pdf), 14–15. For an analysis of the Singapore scheme of arrangement and how it has been used in practice, see Lim (n 3).
[14] In Spain, debtors submitting a reorganisation plan supported by certain creditors (*propuesta anticipada de convenio)* are eligible for a fast-track reorganisation procedure. See Insolvency Act 2020, Article 333. In South Korea, see Debtor Rehabilitation and Bankruptcy Act, Articles 222-224. For a general overview of the regime of pre-packs in South Korea, see Chiyong Rim, 'South Korea' in Corporate Restructuring and Insolvency in Asia (ABLI Legal Convergence Series 2020), 687-688. In Japan, a summary rehabilitation procedure is also available. See Michihiro Mori and Kazuhiro Yanagida, 'Japan: Pre-Packaged Filings and Pre-Filing Arrangements For Sponsorship In Japan' (Mondaq, 30 October 2007) <https://www.mondaq.com/insolvencybankruptcy/53206/pre-packaged-filings-and-pre-filing-arrangements-for-sponsorship-in-japan> accessed 7 September 2021.
[15] These agreements are usually subject to certain requirements and they are not binding on certain creditors. For the Argentinian debt restructuring agreement (*acuerdo extrajudicial de pagos*), see Ricardo W. Beller, 'The APE: Argentina's Prepackaged Debt Restructuring Agreement' (Marval, O'Farrell & Mairal, 2010) (available at <https://www.iiiglobal.org/sites/default/files/media/Argentinas%20Prepackage.pdf>). In Brazil, see Daniel Carnio Costa, 'Recuperação extrajudicial' (2018) Tomo Direito Comercial Edição 1 <https://enciclopediajuridica.pucsp.br/verbete/212/edicao-1/recuperacao-extrajudicial> accessed 7 September 2021. For the out-of-court refinancing agreements in Spain (*acuerdos de refinanciación*), see Ignacio Tirado, 'Out of court debt restructuring in Spain: A modernised framework' (available at https://www.law.ox.ac.uk/sites/files/oxlaw/tirado_modernised_framework.pdf). For an overview of the regime for out-of-court debt restructuring agreements in Italy (*accordi per la ristrutturazione di debiti*), see http://restructuring.bakermckenzie.com/wp-content/uploads/sites/23/2017/01/Global-Restructuring-Insolvency-Guide-12-2016New-Logo-Italy.pdf. In Uruguay, see Insolvency Act 2008, Article 214.

classified as “pre-packs”,[16] this article will use the term “pre-pack” in a narrower sense. Therefore, it will exclude debt restructuring tools that do not necessarily lead to the commencement of a formal reorganisation procedure, as it generally occurs with out-of-court debt restructuring agreements subject to judicial homologation. It will also exclude reorganisation procedures that, while providing certain advantages in terms of speed, are still subject to the formalities and procedural requirements generally existing in an ordinary reorganisation procedure.

2.2.2. Pre-packaged sales

In a pre-packaged sale, a debtor negotiates the sale of all or part of a company’s business or assets *prior* to the commencement of a formal insolvency proceeding. Then, the sales are completed *after* the commencement of the procedure. These types of pre-packs have been very popular in the United Kingdom.[17] In a typical pre-packaged administration in the United Kingdom, the sale of the company’s business or assets is arranged prior to the commencement of an administration procedure, after which the appointed administrator completes the sale, usually on day one of the administration, thereby rescuing the business in whole or in part.[18]

2.2.3. International divergences on pre-packs

Despite the use of a similar terminology, pre-packs – even strictly understood – are conceptually and structurally different across jurisdictions. These international divergences are found in at least three primary aspects: (i) types of pre-packs: (ii) types of companies eligible for a pre-pack; and (iii) regulation of pre-packs.

First, in many countries around the world, including the United States, Singapore, India, and the Philippines, the term “pre-pack” is generally used for pre-packaged reorganisations.[19] In these procedures, companies usually conduct a *debt restructuring* with the purpose of emerging from insolvency with a new financial structure that is more aligned with their actual generation of cash-flows. Therefore, the corporate entity usually remains intact. As a result, these procedures can generally be seen as a form of *corporate* rescue. In other jurisdictions, however, such as the United

[16] Adopting a definition of “pre-packs” that includes the judicial confirmation of a settlement agreed out-of-court that is binding on dissenting creditors, even if it does not lead to the commencement of a formal reorganisation procedure, see Wolfgang Bergthaler, Kenneth H Kang, Yan Liu, and Dermot Monaghan, ‘Tackling Small and Medium Sized Enterprise Problem Loans in Europe’ (2015), IMF Staff Discussion Note 15/04 (available at https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2016/12/31/Tackling-Small-and-Medium-Enterprise-Problem-Loans-in-Europe-42614), p 11. Including as ”pre-packs” summary procedures, such as those existing in Japan and South Korea, see Andreas Bauer, R. Sean Craig, Jose Garrido, Kenneth Kang, Kenichiro Kashiwase, Sung Jin Kim, Yan Liu, and Sohrab Rafiq, ‘Flattening the Insolvency Curve: Promoting Corporate Restructuring in Asia and the Pacific in the Post-C19 Recovery’ (2021) Working Paper No. 2021/016 (available at https://www.imf.org/en/Publications/WP/Issues/2021/01/29/Flattening-the-Insolvency-Curve-Promoting-Corporate-Restructuring-in-Asia-and-the-Pacific-in-49997), pp. 18-20.

[17] See Walton, Umfreville, and Wilson, ‘Pre-pack Empirical Research’ (n 1) 25–26.

[18] Insolvency Practitioners Association, ‘Statement of Insolvency Practice 16: Pre-Packaged Sales in Administrations’ (available at https://insolvency-practitioners.org.uk/uploads/documents/f30389ce35ed923c06b2879fecdb616a.pdf).

[19] See notes 8, 13 and 14.

Kingdom,[20] and more recently Spain,[21] a pre-pack generally refers to a pre-packaged sale of assets. In these procedures, the business is typically saved through a going concern sale, and the insolvent company is ultimately dissolved. Therefore, pre-packs are used as a form of *business* rescue.

Second, jurisdictions can also differ on the types of companies that are potentially eligible for pre-packs. For example, while some countries, such as India,[22] have decided to reserve the use of pre-packs for MSMEs, most jurisdictions around the world, including the United States, the United Kingdom, the Netherlands, the Philippines, Spain and Singapore, do not impose any restriction on the type of companies that are potentially eligible for a pre-pack.

Finally, when it comes to the regulation of pre-packs, certain jurisdictions, such as the United States, Spain, and the Netherlands, have allowed the use of this restructuring tool even if pre-packs are not formally regulated in the insolvency legislation.[23] In the United States and Spain, some courts have issued guidelines to deal with pre-packs.[24] In the United Kingdom, while the disposal of assets to connected parties in administration has been recently regulated,[25] pre-packaged sales have traditionally been governed by a guideline enacted by insolvency practitioners.[26] Therefore, all of these countries subject pre-packs to some form of regulations or generally accepted practices. In India and Singapore, however, pre-packs are regulated in the Insolvency and Bankruptcy Code of 2016,[27] and the Insolvency, Restructuring and Dissolution Act of 2018 respectively.[28] Hence, they are part of the formal insolvency framework.

3. The promises and perils of pre-packs

3.1. Advantages of pre-packs

The primary advantage of a pre-pack is its ability to reduce the length and costs of insolvency proceedings.[29] Insolvency proceedings generate *direct costs* that are mainly associated with the professional fees charged by lawyers, financial advisors

[20] Stephen Phillips and Anna Kaczor, 'The Benefits of UK-style Pre-packs and Comparisons with other Jurisdictions' (2010) 7(5) International Corporate Rescue 328; Mark Norman Wellard and Peter Walton, 'A Comparative Analysis of Anglo-Australian Pre-packs: Can the Means Be Made to Justify the Ends?' (2012) 21(3) International Insolvency Review 143. For an overview of the Spanish pre-packs, see Thery, Garcia-Alaman, Verdugo and Moreno (n 6).

[21] Even though the 2003 Spanish Insolvency Act introduced a type of "fast-track reorganisation procedure" (*propuesta anticipada de convenio*), the formal adoption of pre-packs took place in 2020 when various courts adopted guidelines to facilitate pre-packaged sale of assets. See notes 5 and 16.

[22] The Insolvency and Bankruptcy Code, 2016 (No. 31 of 2016), Chapter III-A.

[23] For an analysis of the pre-packs in the Netherlands, see Springorum and van Pelt (n 5). In Spain, see Thery, Garcia-Alaman, Verdugo and Moreno (n 6). In the United States, see note 8.

[24] In the US guidelines, see United States Bankruptcy Court Southern District of New York, 'Procedural Guidelines for Prepackaged Chapter 11 Cases in the United States Bankruptcy Court for the Southern District of New York' (Order M-454) (2013). In Spain, the judges of the Commercial Courts of Barcelona, Málaga and Baleares have enacted some basic guidelines for pre-packs.

[25] The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021.

[26] Insolvency Practitioners Association (n 18).

[27] See The Insolvency and Bankruptcy Code, 2016 (No. 31 of 2016), Chapter III-A.

[28] Insolvency, Restructuring and Dissolution Act 2018, section 71.

[29] See Elizabeth Tashjian, Ronald C. Lease, and John J McConnell, 'An empirical analysis of pre-packaged bankruptcies' (1996) 40(1) Journal of Financial Economics 135.

and, where relevant, insolvency practitioners.[30] Additionally, a situation of insolvency leads to significant *indirect costs*, regardless of whether a company has initiated a formal insolvency process.[31] These costs include any destruction of value generated as a result of the firm's financial distress, including the loss of reputation, goodwill, employees, lenders, consumers and suppliers.[32]

In a pre-pack, most of the restructuring work is conducted *prior* to the commencement of the insolvency proceedings. Therefore, pre-packs still require the involvement of professionals who advise debtors and creditors. Yet, these costs are lower than those incurred in insolvency proceedings that require the involvement of many professionals over a long period of time.[33] More importantly, by reducing the significant indirect costs generated by a situation of financial distress, typically as a result of the speed and confidential nature of pre-packs, this restructuring tool can help maximise the value of insolvent firms for the benefit of debtors, creditors and society as a whole.

3.2. Risks of pre-packs

Despite the advantages of pre-packs, the use of this restructuring tool can potentially result in certain risks and problems, especially when they are structured as a pre-packaged sale that does not require the approval of the creditors, as it has traditionally occurred in the United Kingdom.[34] First, pre-packaged sales can be used opportunistically by the shareholders to acquire the business or corporate assets without providing creditors with all the protections that traditionally exist in formal insolvency proceedings, including creditor voting.[35] Therefore, it can lead to an opportunistic deviation of assets, and even illegal "phoenix activity" under the laws of certain jurisdictions.[36] Moreover, if the assets are acquired by connected parties who may not offer the best skills to manage the business, or they do not offer the price that an independent bidder would be willing to pay, the sale can lead to a lower likelihood of keeping viable firms alive and reduce the recoveries for the creditors respectively.

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[30] The empirical literature has shown that the direct costs of bankruptcy represent 3 to 4% of the pre-bankruptcy market value of total assets. See Jerold B Warner, 'Bankruptcy Costs: Some Evidence' (1977) 32(2) Journal of Finance 337. See also Ben Branch, 'The costs of bankruptcy: A review' (2002) 11 International Review of Financial Analysis 39, 42–43.

[31] Some studies have found that the costs of financial distress can represent 10 to 20% of the firm value. See Gregor Andrade and Steven N Kaplan, 'How Costly Is Financial (Not Economic) Distress? Evidence from Highly Leveraged Transactions that Became Distressed' (1998) 53 Journal of Finance 1443.

[32] For an analysis of the different indirect costs generated by a situation of financial distress, see Jonathan Berk and Peter DeMarzo, *Corporate Finance* (Pearson, 2nd Edition, Global Edition) pp. 514-516.

[33] Showing the lower direct costs of pre-packs, see Tashjian, Lease, and McConnell, 'An empirical analysis of pre-packaged bankruptcies' (n 29) 143–144. See also Branch (n 30).

[34] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1) 34.

[35] *Ibid*.

[36] As a phoenix is able to burst into flames and rise again from its ashes, the term "Phoenix" is used in the context of pre-packs where the sale is made to a Newco purchaser controlled by the same directors and/or owners of the existing insolvent trading company, see Sidley, 'Taming the Phoenix: New Pre-Pack Regulations Come Into Force' (Sidley, 13 May 2021) (available at https://www.sidley.com/en/insights/newsupdates/2021/05/taming-the-phoenix-new-prepack-regulations-come-into-force). See also Australian Securities & Investments Commission, 'Illegal phoenix activity' (ASIC, 2021) <https://asic.gov.au/for-business/small-business/closing-a-small-business/illegal-phoenix-activity/> accessed 1 September 2021.

Second, for pre-packaged reorganisation procedures that require creditor approval, the speed of pre-packs will likely reduce the time and procedural safeguards that are typically enjoyed by creditors in a formal insolvency proceeding. Therefore, a pre-pack can lead to a reduction in the protection provided to creditors.

Third, pre-packaged sales may be biased towards the interests of secured creditors.[37] This concern is exacerbated where the assets are purchased by existing shareholders using financing that is supplied by existing secured creditors.[38] In those situations, the transaction can often favour the interests of shareholders and secured creditors at the expense of unsecured creditors.[39]

Fourth, managers and insolvency practitioners can also be subject to conflicts of interests in pre-packaged sales. From the perspective of the insolvency practitioners, the fact that they are appointed by the debtor could encourage them to favour the interests of the shareholders.[40] From the perspective of the directors of the company that is conducting a pre-pack, the possibility of losing their jobs may encourage directors to take a soft stance during negotiations to please a potential employer that is acquiring the assets.[41] Other conflicts of interests may arise when the managers acquire the company's assets (that is, in the context of management buyouts),[42] as well as in MSMEs and controlled firms where shareholders are usually involved in the management of the company.[43] Moreover, these conflicts will be exacerbated by the lack of competitive market forces to promote an efficient and transparent sale. This situation may lead to the suboptimal sales of assets, where the company receives lower consideration and therefore the returns to creditors will be reduced.[44]

Finally, from the perspective of the debtor, pre-packs may involve certain legal risks.[45] For instance, in a pre-packaged reorganisation, the debtor faces the risk of not getting the reorganisation plan approved by the court due to the existence of inadequate

[37] Testing this hypothesis and finding no evidence of exploitation of these conflicts of interests, see Andrea Polo, 'Secured Creditor Control in Bankruptcy: Costs and Conflict' (13 September 2012) (available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2084881).
[38] Peter Walton, 'When is Pre-Packaged Administration Appropriate - A Theoretical Consideration' (2011) 20 Nottingham L.J. 1, 10–11.
[39] *Ibid*.
[40] Peter Walton, 'Pre-Packaged Administrations – Trick or Treat?' (2006) 19(8) Insolvency Intelligence 113, 120.
[41] *Id*, citing Vanessa Finch, 'Pre-packaged administrations: bargains in the shadow of insolvency or shadowy bargains' (2006) Journal of Business Law 568, 574.
[42] The insolvency practitioners advising on a pre-pack to a newco with set out by former directors of the debtor suggest the possibility of a conflict of interest, see *Ve Vegas Investors IV LLC v Shinners* [2018] EWHC 186 (Ch).
[43] Aurelio Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms' (International Insolvency Review, 2021) (available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3715654).
[44] Alexandra Kastrinou and Stef Vullings, '"No Evil is Without Good": A Comparative Analysis of Pre-pack Sales in the UK and the Netherlands', (2018) 27(3) International Insolvency Review 320, 326; Vanessa Finch, *Corporate Insolvency Law* (Cambridge University Press, 2009), 462; Stephen Davies QC, 'Pre-pack – He Who Pays the Piper Calls the Tune' (2006) Recovery (Summer), 16.
[45] Finch (n 44), 458, citing Mark D. Plevin, Robert T. Ebert and Leslie A. Epley, 'Pre-packaged Asbestos Bankruptcies: A Flawed Solution' (2003) 44 South Texas Law Review 883, 888-889.

disclosure to creditors.[46] If so, the debtor may be required to resolicit acceptances, resulting in delays to the confirmation of a plan,[47] undermining some of the benefits of pre-packs.[48] Moreover, in a pre-packaged sale, the debtor may also face the risk of having the sale challenged *ex post*.[49]

4. Unlocking pre-packs

4.1. Types of companies conducting a pre-pack

In some countries, such as India, the pre-pack is a restructuring tool that is only available to MSMEs.[50] In most of the jurisdictions that allow pre-packs, however, this restructuring mechanism can be used by any company. Some empirical studies in the United Kingdom have shown that pre-packs are frequently utilised by MSMEs,[51] which have relatively small asset value,[52] are incorporated between 5 to 15 years prior to entering administration,[53] have a secured indebtedness of under £250,000,[54] and have an unsecured indebtedness below £500,000.[55] Therefore, at least in the United Kingdom, the data indicates that pre-packs are generally used by small and relatively young enterprises.

In Singapore, since the adoption of pre-packs in 2017, this restructuring tool has been used by all types of companies, including large enterprises such as PT MNC Investama and Modernland Realty.[56] Therefore, the success of these high-profile restructuring cases show that the new pre-packaged scheme of arrangement can also serve as a valuable restructuring mechanism for large companies. Regardless of the size of the company using this restructuring tool, a pre-pack will generally be more

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[46] Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (Edward Elgar Publishing, 2008), 105. See also *In re City of Colorado Springs* 177 B.R. 684, 691 (Bankr. D. Colo. 1995).
[47] McCormack (n 46).
[48] Finch (n 44), 458, citing Plevin, Ebert and Epley, 'Pre-packaged Asbestos Bankruptcies' (n 45), 889.
[49] The UK court has signalled that an ex post challenge by a "sufficiently aggrieved creditor" is possible, see *Re Hellas Telecommunications (Luxembourg) II SCA* [2009] EWHC 3199 (Ch) at [8]. However, unsecured creditors are "not known for exercising the statutory rights at their disposal", see Adrian J. Walters, 'Statutory Erosion of Secured Creditors' Rights: Some Insights from the United Kingdom' (2015) 2 University of Illinois Law Review 543, 569.
[50] See The Insolvency and Bankruptcy Code, 2016 (No. 31 of 2016), section 54A(1). The definition of a micro, small and medium enterprise for the purpose of the Insolvency and Bankruptcy Code is provided at The Micro, Small And Medium Enterprises Development Act, 2006, section 7.
[51] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 12–13. See also Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 24 and 26.
[52] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 24 and 26. See also Alan Katz and Michael J Mumford (2008) A Study of Administration Cases, The Insolvency Service, London.
[53] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 11.
[54] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 24.
[55] *Id*, 26.
[56] The turnaround of PT MNC Investama included the restructuring of US$231 million (S$311 million) of secured notes. See K.C. Vijayan, 'Singapore well-placed to meet rise in debt restructuring demand amid Covid-19' (Straits Times, 9 November 2020) <https://www.straitstimes.com/singapore/singapore-well-placed-to-meet-rise-in-debt-restructuring-demand-amid-covid-19> accessed 1 September 2021. Modernland Realty applied in July 2021 for court sanction of a pre-packaged scheme to restructure two sets of notes worth more than USD400 million. See Emmanuel Chua, Daitza Hon and Yap Yong Li, 'Forum shopping in Asian restructuring' (Asian Business Law Journal, 24 August 2021) <https://law.asia/forum-shopping-asian-restructuring/> accessed 1 September 2021.

desirable for companies with concentrated debt structures and a small number of creditors.[57] In companies with dispersed creditors, the debtor will be exposed to a higher risk of opportunistic behaviour by individual creditors. Therefore, they may be required to use some of the additional tools provided in the insolvency legislation.

In other countries, such as the United States, the use of pre-packs has been very popular in the past decades.[58] Among the types of companies using pre-packs, there is anecdotal evidence suggesting that this restructuring tool can work for companies other than MSMEs. Large companies that have successfully used a pre-pack in the United States include Belk Inc,[59] HighPoint Resources Corp,[60] Mood Media Corp,[61] Sungard Availability Services Capital Inc,[62] and Fullbeauty Brands Inc.[63]

4.2. Type of buyers in pre-packaged sales

In a typical *pre-packaged reorganisation* such as those that exist in the United States and Singapore, the company's assets are not generally sold. Instead, the pre-pack typically consists of a reorganisation plan proposing a restructuring of the debtor's financial structure.[64] In a pre-packaged sale, however, there is an *actual* sale of assets. In the United Kingdom, it has been shown that the buyer of the company's assets are generally connected parties.[65]

4.3. Other features of pre-packs

The empirical literature has also analysed other important features of pre-packs. First, in terms of the *length* of pre-packs, some studies conducted in the United Kingdom have shown that the majority of pre-packs have been completed within 12 months.[66]

[57] Lim (n 3).
[58] See note 2.
[59] Douglas M. Foley, Sarah B. Boehm, Stephanie Jane Bentley, 'Usain "Belk" — The Fastest Prepack Alive?' (McGuireWoods, 5 March 2021) <https://www.mcguirewoods.com/client-resources/Alerts/2021/3/usain-belk-the-fastest-prepack-alive> accessed 5 September 2021.
[60] Sebastian Tong, 'HighPoint Files for Bankruptcy, Set to Be Bought by Bonanza' (Bloomberg, 15 March 2021) <https://www.bloomberg.com/news/articles/2021-03-14/shale-driller-highpoint-resources-files-for-bankruptcy> accessed 5 September 2021.
[61] Business Wire, 'Mood Media Enters Into Agreement with Supermajority of Lenders on Terms of a Comprehensive Prepackaged Financial Restructuring Plan' (Business Wire, 26 June 2020) <https://www.businesswire.com/news/home/20200626005171/en/Mood-Media-Enters-Into-Agreement-with-Supermajority-of-Lenders-on-Terms-of-a-Comprehensive-Prepackaged-Financial-Restructuring-Plan> accessed 5 September 2021.
[62] Petition, 'New Chapter 11 Filing - Sungard Availability Services Capital Inc.' (Petition, 1 May 2019) <https://www.petition11.com/cases/2019/4/5/new-chapter-11-filing-sungard-availability-services> accessed 5 September 2021.
[63] *Ibid*.
[64] Some authors, however, define reorganisations as "hypothetical" sales. See Douglas Baird, 'The Uneasy Case For Corporate Reorganizations' (1986) 15(1) Journal of Legal Studies 127.
[65] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 40–47.
[66] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 27–28.

In the United States, while there is anecdotal evidence of pre-packs being conducted within 24 hours,[67] a typical pre-pack lasts 77 days on average.[68]

Second, the pre-packaged sales conducted in the United Kingdom are typically subjected to a *valuation*. Namely, it has been shown that businesses were valued in 83.7% of pre-packaged sales,[69] and other empirical studies have confirmed that an independent valuation has been conducted in the overwhelming majority of pre-packs.[70]

Third, in terms of the *consideration* received in exchange for the sale of assets, 50% of the pre-packaged sales conducted in the United Kingdom included an element of deferred consideration.[71] This includes personal guarantees from the directors,[72] as well as other forms of security such as fixed charges over property.[73]

Fourth, in the majority of cases of pre-packaged sales in the United Kingdom, the administrators reported that *marketing* was carried out prior to the pre-packaged sale.[74] However, the data is based on self-reporting by the administrators and there appears to be a wide disparity as to the level of marketing taking place.[75]

5. Assessing the impact of pre-packs

5.1. Impact on creditor recoveries

In countries with pre-packaged reorganisations such as the United States and Singapore, the expected return to creditors is based on the reorganisation proposal. After analysing a variety of factors, including the viability of the business, the reliability of the management team, the credibility of the figures presented by the debtor, and the hypothetical scenario if the agreement fails, creditors will ultimately decide on whether they want to support the reorganisation plan. In countries that embrace a system of pre-packaged sales, however, the lower involvement of the creditors may result in a higher risk of reduction of their recoveries.

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[67] See for example Pat Holohan, 'COURT: Belk judge confirms prepack plan on first day, with conditions' (Debtwire, 24 February 2021) <https://www.debtwire.com/info/court-belk-judge-confirms-prepack-plan-first-day-conditions> accessed 2 September 2021.

[68] See Bauer, Craig, Garrido, Kang, Kashiwase, Kim, Liu, and Rafiq (n 16), 20, footnote 12. These authors reported that while the average ordinary reorganisation procedure in the US during the period 2011-2018 lasted 504 days, pre-packaged reorganisations for the same period lasted only 77 days on average, and pre-arranged bankruptcy cases lasted 219 days on average. Between the period October 1986 and June 1993, however, some studies showed that the average pre-packaged reorganisation in the US lasted 21.6 months. Based on this evidence, the authors argued that the speed of pre-packs can often be exaggerated. See Lynn M. LoPucki and Joseph W. Doherty, 'Why are Delaware and New York Bankruptcy Reorganizations Failing?' (2002) 55(6) Vanderbilt Law Review 1933.

[69] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 50.

[70] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 23.

[71] *Id*, 20.

[72] *Ibid*.

[73] *Ibid*.

[74] *Id*, 45.

[75] *Id*, 21.

The impact of pre-packaged sales on the recovery of creditors has been analysed in various empirical studies in the United Kingdom. In the context of *secured creditors*, it has been shown that the average return received in a pre-pack was 59.1%,[76] while the average return of secured creditors in a business sale in an ordinary administration procedure was 27.5%.[77] Furthermore, the probability of obtaining a return of at least 50% of the secured debt is higher in pre-packs compared to business sales in a regular administration procedure.[78] Thus, the evidence shows that secured creditors are generally better off in a pre-pack.

On the other hand, the evidence shows that *unsecured creditors* benefit slightly more from an ordinary administration procedure compared to a pre-pack. Namely, it has been shown that the average return to unsecured creditors was 2% in pre-packs while the average return to unsecured creditors was 4% in a business sale in an ordinary administration procedure.[79] Moreover, since not all insolvency cases generate recoveries for the creditors, it was also shown that where there were recoveries for the creditors, the average return to unsecured creditors was also higher in a business sale in a regular administration procedure.[80] Finally, the likelihood of a zero return is 6% higher in pre-packs than in business sales in an ordinary administration procedure.[81] Therefore, while a zero percent return remains the most likely outcome for unsecured creditors in both types of sales,[82] unsecured creditors are slightly worse off in pre-packs compared to a business sale in an ordinary administration procedure. The divergences in the returns to unsecured creditors are more relevant, however, when the assets are sold to *connected parties* – either in an ordinary administration procedure or through a pre-pack. In those cases, unsecured creditors seem to receive lower returns.[83] However, other empirical studies have challenged the fact that unsecured creditors are worse-off, even in the context of pre-packaged sales to connected parties.[84] Therefore, the evidence is not conclusive.

5.2. Impact on the survival of businesses

In the United Kingdom, it has been shown that compared to pre-packs, there is a higher likelihood of failure when a business is sold in an ordinary administration

[76] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 60.
[77] *Ibid*.
[78] Returns of over 50% are recorded in 74% of the pre-pack sample, as compared to 66% of the business sale sample, see Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 61.
[79] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 64.
[80] The average creditor dividend is 7.22% for pre-packs, while the average creditor dividend is 13.06% for business sales in ordinary administration, though it should be noted the latter data "*appears to be skewed by a two significant larger distributions*", and the median value for returns is lower in business sales in ordinary administration as compared to a pre-pack; see Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 32 and 65.
[81] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 65–66.
[82] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 65–66; see also Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 32 and 65, both highlighting that in more than 50% of both pre-pack and business sales in ordinary administration in cases lead to no dividends distributed to unsecured creditors.
[83] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 33 and 66.
[84] Polo (n 37).

procedure.[85] In addition, for both types of business sales, there was a greater chance of failure in situations where the business is sold to a connected party.[86] In fact, in the context of pre-packs, the number of failures within 36 months when the business was sold to connected purchasers was more than three times that of the number of failures within 36 months when the business was sold to non-connected purchasers.[87] Additionally, for both types of business sales, the failure rate is higher where deferred consideration is present.[88]

In the United States, it was found that debtors who reorganised by way of pre-packs had lower post-bankruptcy earnings than those who reorganised without pre-packs.[89] Therefore, it has been suggested that pre-packaged organisations are more likely to fail than non-pre-packaged reorganisations.[90]

5.3. Preservation of jobs

The evidence in the United Kingdom has shown that when it comes to the preservation of jobs, pre-packs have been more successful than ordinary business sales in administration.[91] Namely, it has been shown that 92% of pre-packs resulted in a 100% employment preservation rate, and only 2% resulted in a 100% redundancy rate. Conversely, only 65% of business sales in regular administration procedures resulted in a transfer of the entire workforce while 16% resulted in a 100% redundancy rate prior to the transfer.[92] The evidence from other jurisdictions, such as the Netherlands, also seems to support the effectiveness of pre-packs for the preservation of jobs.[93]

6. Policy recommendations for the adoption or improvement of the regulatory framework of pre-packs

6.1. Country-specific factors affecting the need to favour pre-packs

While pre-packs can create many advantages, they also entail certain risks. Therefore, despite the global trend embracing the use of pre-packs, the adoption of this restructuring tool should be carefully examined. First, regulators should assess whether the adoption of a pre-pack procedure is really needed in their jurisdictions.

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[85] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 80. However, the evidence does not seem conclusive. See, for instance, Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 75-78.

[86] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 50–52 and 69. See also Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 79, which states that for business sale in administrations, the survival rate for connected sales was 58%, while the survival rate for unconnected sales was 71.9%. For pre-packs, the survival rate for connected sales was 51.4%, while the survival rate for unconnected sales was 71.5%.

[87] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 38.

[88] Walton, Umfreville, and Wilson, 'Pre-pack Empirical Research' (n 1), 39 and 78.

[89] LoPucki and Doherty (n 68), 1972.

[90] *Ibid*.

[91] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 71.

[92] *Id*, at p 70.

[93] See Springorum and van Pelt (n 5), referencing Steffie van den Bosch, 'De pre-pack in de Nederlandse praktijk: een empirisch onderzoek vanuit economisch perspectief' (available at http://www.uitgeverijparis.nl/scripts/read_article_pdf_li.php?id=1001391709&cks=6d6722e8bdcfb9cc9c533f7b5e93e8326ba22b4c).

For instance, the adoption of a pre-pack might not be needed in jurisdictions with other attractive hybrid procedures such as the enhanced scheme of arrangement existing in Singapore, the new restructuring plan adopted in the United Kingdom, and the restructuring procedure envisioned by the EU Directive on Preventive Restructuring Frameworks.[94]

Also, if the adoption of pre-packs is mainly driven by the need to provide small and medium enterprises with an efficient reorganisation procedure, the implementation of this restructuring tool may not be necessary in jurisdictions with simplified insolvency frameworks for MSMEs, such as Myanmar and Australia.[95] Similarly, the need for pre-packs will be reduced in jurisdictions with an attractive environment for workouts due to several factors, including: (i) the successful use of "informal norms" or "good practices" for out-of-court restructuring;[96] (ii) the existence of a market mainly formed by repeated players incentivised to respect the informal rules of the game in an out-of-court debt restructuring;[97] (iii) the prevalence of companies with concentrated debt structures, usually as a result of the existence of many MSMEs and a bank-based financial system;[98] and (iv) the adoption of incentives for the facilitation of workouts, such as the tax deductibility of any debt forgiveness ("haircut") achieved in a workout or the use of tax credits granted to creditors accepting a haircut.[99]

In jurisdictions with attractive environment for workouts and hybrid procedures, while a pre-pack can still bring some benefits, the adoption of this restructuring tool will not be as essential as in countries with a burdensome one-size-fits-all insolvency process. Therefore, if pre-packs can create certain risks, and the comparative advantage of

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[94] For Singapore, see Insolvency, Restructuring and Dissolution Act 2018, Part 5. For the UK restructuring regime introduced in 2020, see Companies Act 2006, Part 26A. For the restructuring procedure in EU, see Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132.

[95] For the simplified insolvency framework in Australia, see Corporations Act 2001 (Cth), Part 5.3B. For Myanmar, see Gurrea-Martinez, Implementing an Insolvency Framework for Micro and Small Firms (n 43).

[96] In many countries, such as the United Kingdom, the use of informal norms favouring workouts, known as "The London Approach", mainly target large companies with concentrated debt structures. See John Armour and Simon Deakin, 'Norms in Private Insolvency: The "London Approach" to the Resolution of Financial Distress' (2001) 1(1) Journal of Corporate Law Studies 21. However, pre-packs are often used by MSMEs. Therefore, pre-packs are expected to be more needed and utilised if, as it happens in the United Kingdom, small companies do not take advantage of the informal norms favouring workouts existing for large companies.

[97] Armour and Deakin (n 96), 40-46. See also John Armour, Brian R. Cheffins, and David A. Skeel, Jr. 'Corporate Ownership Structure and the Evolution of Bankruptcy Law: Lessons from the United Kingdom' (2002) 55(6) Vanderbilt Law Review 1699, 1759.

[98] Armour, Cheffins, and Skeel, Jr. (n 97), 1707. See also Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms' (n 43).

[99] Aurelio Gurrea-Martinez and Vincent Ooi, 'The Tax Treatment of Haircuts in Financial Reorganizations' (2020) 27 Revenue Law Journal 1; Federico J. Díez, Romain Duval, Jiayue Fan, José Garrido, Sebnem Kalemli-Özcan, Chiara Maggi, Soledad Martinez-Peria, and Nicola Pierri 'Insolvency Prospects Among Small and Medium Enterprises in Advanced Economies: Assessment and Policy Options' (2021), IMF Staff Discussion Notes No. 2021/002, (available at https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138). See also Garrido (n 7) at 23.

pre-packs is reduced in those jurisdictions, regulators should examine more carefully whether the implementation of a pre-pack will be economically desirable.

Second, even if a country has a one-size-fits-all insolvency process, the desirability of adopting a pre-pack will vary depending on the efficiency of insolvency proceedings in a particular jurisdiction. For instance, while a pre-pack can save some costs of financial distress in countries with efficient insolvency frameworks, such as the United States, Germany and Japan,[100] the benefits of adopting a pre-pack – and more generally out-of-court solutions – will likely be greater in countries with inefficient insolvency frameworks, which generally occurs in emerging economies.[101]

6.2. The design of the regulatory framework for pre-packs

6.2.1. General features of the pre-pack

If it is determined that pre-packs should be introduced in a particular jurisdiction, the next challenge will consist of the design of the framework for pre-packs. To that end, countries should consider several aspects. First, they will need to decide whether, as it happens in Singapore and India, pre-packs are regulated in the insolvency legislation or, following the model existing in the United Kingdom and the United States, pre-packs are regulated through informal practices or procedural rules issued by courts. In jurisdictions without a traditional history of pre-packs, the formal regulation of pre-packs can probably provide more certainty for debtors and creditors.

Second, regulators should decide whether a pre-pack will be available to all types of firms or, as India has done, they will be limited to MSMEs. In jurisdictions with fast and low-cost reorganisation procedures for small companies, such as the United States, Australia and temporarily Singapore, pre-packs will likely to be mainly used by larger companies. In the United Kingdom, however, it has been shown that pre-packs are frequently used by MSMEs.[102] This is consistent with the fact that the United Kingdom, like most countries around the world,[103] do not provide attractive restructuring frameworks for MSMEs, and therefore a pre-pack can be a reasonable solution in the event of insolvency. From a policy perspective, since pre-packs can indeed be particularly useful for MSMEs (especially in countries without an attractive insolvency framework for small companies), and they can still serve as an attractive tool for many large companies, as seen from the experiences of the United States and Singapore, making pre-packs available to all types of companies seems to be a more desirable solution.

Third, regulators should also consider whether a financial requirement should be imposed for the initiation of a pre-pack. To that end, many jurisdictions around the

[100] For data on the efficiency of these countries' insolvency regimes, see The World Bank, Doing Business, 'Resolving insolvency' <https://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency> accessed 3 September 2021.
[101] Aurelio Gurrea-Martinez, 'Insolvency Law in Emerging Markets', Ibero-American Institute for Law and Finance, Working Paper 3/2020 (available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3606395).
[102] See part 4.1 above and note 51.
[103] Gurrea-Martinez, 'Implementing an Insolvency Framework for Micro and Small Firms' (n 43).

world impose various entry requirements for the initiation of a reorganisation procedure, and therefore a similar policy could be adopted for pre-packs.[104] If those requirements include financial conditions that are reviewed by courts, however, the imposition of these requirements may delay the initiation of the procedure, undermining the primary advantage of a pre-pack. Moreover, in countries without experienced and well-functioning courts, this assessment may bring additional problems, including further delays, lack of expertise to assess the financial conditions of the company, and even corruption in certain countries.[105] Therefore, companies should not be subject to any formal financial requirement for the use of a pre-pack. However, the financial situation of the company should be disclosed to the creditors while the pre-pack is negotiated, and a pre-pack should be subject to either creditor voting or the ability to be challenged *ex post*. If a debtor is solvent, the creditors might be reluctant to approve a pre-pack, or they may have incentives to challenge the pre-pack. These protections, along with the fact that solvent debtors are unlikely to seek to conduct a debt restructuring, will likely reduce the opportunistic behaviour of debtors potentially using a pre-pack.

Fourth, jurisdictions should assess whether a pre-pack should consist of a pre-packaged reorganisation, a pre-packaged sale, or both. For that purpose, it is important to consider the different goals of insolvency law, and how these goals can be achieved.[106] Where a company is not economically viable, the primary goal of insolvency law should consist of ensuring that the company is liquidated in an efficient and orderly manner.[107] For a viable but inefficiently managed firm, the goal ought to be the preservation of the business, and this can be achieved through a going concern sale.[108] In those cases, a *pre-packaged sale* can generally be more desirable than a pre-packaged reorganisation, since the former usually implies a change in the management team. In circumstances where the company is economically viable not only due to its business model but also because of the credibility and expertise of the management team, the value of the firm will be maximised if the company is kept alive in the hands of the existing managers.[109] In those situations, a *pre-packaged reorganisation* will provide a more desirable solution.

Hence, since a pre-packaged sale or a pre-packaged reorganisation can be more or less desirable depending on the circumstances, both options should ideally be available, provided that sufficient creditor safeguards are introduced. In the absence of such protections, the adoption of any form of pre-packs might end up doing more

[104] Business Today India, 'Pre-packaged resolution for MSMEs: Govt sets minimum default threshold at Rs 10 lakh' (Business Today India, 7 April 2021) <https://www.businesstoday.in/latest/economy-politics/story/pre-packaged-resolution-for-msmes-govt-sets-minimum-default-threshold-at-rs-10-lakh-292814-2021-04-07> accessed 3 September 2021.
[105] Emphasising this aspect in some emerging markets, see Gurrea-Martinez, 'Insolvency Law in Emerging Markets' (n 101).
[106] Aurelio Gurrea-Martinez, 'The Role of Corporate Insolvency Law in the Promotion of Economic Growth' (Singapore Global Restructuring Initiative, 1 July 2021) (available at https://ccla.smu.edu.sg/sgri/blog/2020/07/01/role-corporate-insolvency-law-promotion-economic-growth).
[107] World Bank, Principles for Effective Insolvency and Creditor/Debtor Regimes' (World Bank, 2021) 7.
[108] Gurrea-Martinez, 'The Role of Corporate Insolvency Law in the Promotion of Economic Growth' (n 106).
[109] *Ibid*.

harm than good because lenders might respond by imposing more stringent conditions to extend credit. Therefore, in addition to other potential costs and challenges created by a pre-pack regime,[110] the adoption of pre-packs may reduce firms' access to finance and the promotion of economic growth.[111]

6.2.2. Specific features and safeguards in pre-packaged reorganisations

The specific mechanisms to protect creditors will depend on a variety of factors, including the institutional framework of the country and the type of pre-pack to be implemented. If the pre-pack consists of a *pre-packaged reorganisation*, creditors are supposed to vote or at least provide their formal support to the debtor.[112] In those cases, the support from the majority of creditors needed for the approval of a plan, along with a system of proper disclosure, should provide enough safeguards to the creditors. Additionally, jurisdictions adopting a pre-packaged reorganisation can also consider the mandatory appointment of an insolvency practitioner acting as a *supervisor* to provide further protection to creditors. Moreover, by providing expertise and credibility to the process, the appointment of a supervisor can result in a greater chance of success for the benefit of debtors and creditors.

However, the mandatory appointment of a supervisor will only be desirable when they can add value to the process. Unfortunately, the value eventually added by supervisors will depend on a variety of firm-specific and country-specific factors. For example, in countries without a sophisticated body of insolvency practitioners, the appointment of a supervisor may end up doing more harm than good.[113] Also, in the specific contact of certain firms (e.g. many MSMEs), a supervisor might not be needed. Therefore, as a general rule, it cannot be argued that the mandatory appointment of an insolvency practitioner will add value. Nonetheless, the mandatory appointment of an insolvency practitioner will *always* create costs. Moreover, if the involvement of an insolvency practitioner can create value, debtors should have incentives to appoint a supervisor. Even if they do not, it should be kept in mind that pre-packs are often negotiated without a statutory moratorium protecting the debtor from creditors' legal actions. Therefore, creditors are expected to have significant bargaining power. As a result, whenever the appointment of a supervisor is needed, creditors will have the power to ask the debtor to appoint a supervisor.

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[110] See section 3.2.

[111] See John Armour, Antonia Menezes, Mahesh Uttamchandani & Kristin van Zwieten, 'How do Creditor Rights Matter for Debt Finance? A Review of Empirical Evidence' in *Research Handbook on Secured Financing of Commercial Transactions* (Frederique Dahan ed., Edward Elgar, 2015), pp 3–25. See also Gurrea-Martinez, 'The Role of Corporate Insolvency Law in the Promotion of Economic Growth' (n 106).

[112] In the absence of an actual vote, creditors may support the pre-pack by way of signed ballot forms. Such ballot forms are provided in the Pre-packaged Chapter 11 Case Ballot Form attached to the Procedural Guidelines for Pre-packaged Chapter 11 Cases in the United States for the Southern District of New York, and they have also been used in some pre-packs in Singapore. See Lim (n 3). See also Marcia L. Goldstein, 'Prepackaged Chapter 11 Case Considerations and Techniques' (International Insolvency Institute 8th Annual International Insolvency Conference, June 9 2008) 23–26 (available at https://www.iiiglobal.org/sites/default/files/marciagoldstein.pdf).

[113] Aurelio Gurrea-Martinez, 'Insolvency Law in Emerging Markets', Ibero-American Institute for Law and Finance, Working Paper 3/2020 (available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3606395).

As a result of these factors, the *mandatory* appointment of a supervisor does not seem to be a desirable policy, at least during the pre-petition phase of the pre-pack. However, once a debtor has initiated the reorganisation procedure and is awaiting the confirmation of the plan, the mandatory appointment of an insolvency practitioner can be more justified – especially if the pre-pack is not approved within a short period of time and the debtor needs to stay in a formal insolvency proceeding for a longer period. In those situations, the debtor will enjoy the tools and protections provided by insolvency law. Therefore, due to the greater risk of opportunism of debtors *vis-à-vis* creditors, the appointment of a supervisor can be more desirable, especially in countries with sophisticated insolvency practitioners. This solution will also be more consistent in jurisdictions that require the appointment of an insolvency practitioner in reorganisation procedures.

Finally, another solution that can be potentially considered for the protection of creditors is the creation of a *committee of creditors.* This solution can make sense in large corporate reorganisations with dispersed and rationally apathetic creditors, especially if an insolvency practitioner is not appointed –as it generally happens in a corporate reorganisation in the United States. In those cases, creditors should be entitled to appoint a small committee of creditors that can act as an intermediary between the debtors and the whole body of creditors represented in the creditors' meeting. In situations of small and medium enterprises with a few concentrated creditors, however, the existence of a creditors committee might not be needed. Moreover, if as it happens in certain jurisdictions (e.g., United States), the fees and expenses generated by the committee of creditors are covered by the debtor, this solution can end up reducing the recoveries for the creditors.

6.2.3. Specific features and safeguards in pre-packaged sales

6.2.3.1. Solutions suggested or traditionally adopted in the United Kingdom

A pre-packaged sale of assets may imply greater risks if, as it happens in the United Kingdom, the support of the creditor is not required for the sale. The solution traditionally used in the United Kingdom to deal with this problem has mainly consisted of the appointment of an administrator and the imposition of certain duties and disclosure obligations.[114] However, this approach has been criticised on several grounds, including the existence of conflict of interests, the lack of transparency in the process, and the insufficient involvement of creditors.[115]

The academic literature has suggested various proposals for the improvement of the regulatory framework for pre-packs in the United Kingdom, especially when the assets are sold to connected parties. First, it has been argued that the pre-pack can adopt a procedural mechanism from the regulatory framework for management buyouts in the

[114] Insolvency Practitioners Association (n 18).

[115] Bo Xie, 'Role of insolvency practitioners in the UK pre-pack administrations: challenges and control' (2012) 21(2) International Insolvency Review 85, 89–94. For a variety of solutions on improving the regulatory framework of pre-packs in the United Kingdom, see Chris Umfreville, 'Review of the pre-pack industry measures: Reconsidering the connected party sale before the sun sets' (available at https://publications.aston.ac.uk/id/eprint/32919/1/Review_of_the_pre_pack_industry_measures.pdf).

context of solvent companies.[116] After all, the same fundamental problem of inside information exists in sales of both solvent and insolvent companies to connected parties.[117] To that end, the UK Takeover Code deals with this problem by requiring the connected party buyer to furnish to the company's independent directors, upon request, copies of all information they have sent to their financiers.[118] The rule proposed for the improvement of the regulatory framework for pre-packs would require a connected party bidder to disclose to the debtor company's independent directors, on request, all information that they have sent to their financiers, thereby reducing the extent to which the insiders are able to use private information to their own advantage.[119] This solution, however, would only work for companies that are required to have independent directors. Therefore, since the vast majority of firms are MSMEs which do not have independent directors, another solution should be adopted for such firms.

Second, it has also been suggested that informing creditors about the identity of the purchasers should be an essential requirement of any pre-packaged sales.[120] Additionally, it has been pointed that that it should be mandatory for advisers to file a statement to the court giving fundamental details of the pre-pack, including: (i) the date of first instruction; (ii) the reasons for the pre-pack; (iii) the period of marketing; (iv) all valuations received; (v) the terms of sale; and (vi) the total fees of the adviser's firm and the source of those fees.[121]

Third, other authors have suggested that creditors should be allowed to challenge a sale within a short period of time after the transaction takes place.[122] Moreover, this approach differs from pre-scrutiny in not slowing down the pre-pack process and sought-after sales.[123] Therefore, it can provide more protections to creditors without undermining some of the benefits of a pre-pack.

Fourth, it has also been argued that administrators should only be allowed to take expenses incurred prior to formal appointment once these have been expressly authorised by the creditors within the administration proceedings.[124] This proposal is designed to not only ensure transparency but also more effective creditor scrutiny of the administrator's actions.[125]

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[116] John Armour, 'The Rise of the "Pre-Pack": Corporate Restructuring in the UK and proposals for reform' in Austin and Aoun (n 1), p 27.
[117] *Ibid*.
[118] *Ibid*.
[119] *Id*, at p 30.
[120] Frisby, 'A Preliminary Analysis of Pre-packaged Administrations' (n 1), 31.
[121] Davies (n 44).
[122] Vanessa Finch, 'Corporate Rescue: A game of three halves' (2012) 32(2) Legal Studies 302, 319.
[123] *Id*, citing Turnaround Management Association President, Bryan Green's letter to the *Financial Times* on 5 April 2011, where Bryan Green proposes a "14-day period following the pre-pack, during which all stakeholders can make any objections they might have heard" <https://www.ft.com/content/4af8cbfe-5f0b-11e0-a2d7-00144feab49a> accessed 3 September 2021.
[124] Finch (n 44), 469.
[125] Desmond Flynn, 'Pre-pack Administrations – A Regulatory Perspective' (2006) Recovery (Summer). See also Peter Walton, 'Pre-appointment administration fees – papering over the cracks in pre-packs?' (2008) 21(5) Insolvency Intelligence 72.

6.2.3.2. New regulatory framework for pre-packs in the United Kingdom

Due to the criticism of the regulatory framework of pre-packs that traditionally exist in the United Kingdom, the Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021 ("the Administration Regulations"), which came into force on 30 April 2021, has adopted additional safeguards for creditors in the context of sale of assets to *connected* parties. Namely, the Administration Regulations states that an administration cannot execute a pre-pack if all of the following requirements apply: (i) the sale (or other form of disposal, including hiring out) is of all or substantially all of the insolvent company's business or assets; (ii) it is within the first 8 weeks of an administration; (iii) the disposal is to one or more persons connected with the company; (iv) either the administrator has not obtained the approval of creditors or the purchaser has not obtained and provided a "qualifying report" of an evaluator.[126]

In practice, the most relevant element for the protection of creditors is found in the need to obtain the approval of creditors *or* a "qualifying report" of an evaluator. The Administration Regulations also sets out the approach that must be taken when evaluators give their opinion on a proposed pre-pack administration. The evaluator's written opinion must be commissioned by the purchaser and should include: (i) 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"; (ii) the evaluator's reasons for coming to their opinion; (iii) the consideration that will be paid; and (iv) the identity of the connected person and their connection to the company.[127]

This solution can be criticised on several grounds. First, since creditor approval is not always required, it is unlikely that debtors will defer the transaction to a creditor vote. Therefore, the parties with more skin in the game will not always be heard, even in the context of sales to connected parties that, as shown by the empirical literature, lead to suboptimal outcomes for the creditors. Second, despite the introduction of an evaluator's opinion,[128] an administrator is not bound to accept the evaluator's opinion.[129] Therefore, debtors may attempt to manipulate the process by soliciting multiple evaluator's opinions in an attempt to obtain a favourable report. As a result, this system may generate a problem of "opinion shopping".[130] Third, the evaluation process may also hinder some of the benefits of the pre-pack, including the speed and costs – even if those costs are borne by the buyer.[131] Fourth, the qualifications of the

[126] The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021, Regulation 3.
[127] *Ibid*
[128] *Id*, at Chapter 3.
[129] The Administration (Restrictions on Disposal etc. to Connected Persons) Regulations 2021, Regulation 7(h).
[130] Alex Ralph, 'Pre-pack reform plan is flawed, say experts', (The Times, 20 October 2020) <https://www.thetimes.co.uk/article/pre-packs-reform-plan-is-flawed-say-experts-nppl3bgrv> accessed 5 September 2021.
[131] Inga West and Rebecca James, 'Latest Pre-pack reforms: independent opinion required for administration sales to connected persons' (2020) 6 Corporate Rescue and Insolvency 209. See also Stuart Hopewell, 'Evaluations: from an opinion to a qualified judgment?' (2021) 3 Corporate Rescue and Insolvency 79.

evaluator seems insufficient or too vague.[132] Therefore, it is not clear whether they will have the technical expertise required for this type of report. Finally, while the new framework is expected to enhance the transparency of pre-packaged sales to connected parties, it does not deal with sales to unconnected parties. Therefore, it is far from clear that the new regulatory framework for pre-packs in the United Kingdom will provide effective protection to creditors – especially unsecured creditors.

6.2.3.3. Enhancing the regulatory framework for pre-packaged sales

Due to the higher risks that are associated with pre-packaged sales, regulators should ideally provide various protections to the creditors. First, the sales to connected parties should always be subject to *creditor approval*. Even though it can be argued that a system of *ex ante* approvals may delay the process, which undermines one of the primary advantages of pre-packs, the rise of new technologies can address this problem. Indeed, by facilitating the use of technologies, this approval can be obtained without causing any significant delay in the process. Therefore, preventing the actors with more skin in the game from being involved in this decision does not seem justified these days, especially in the context of sales to connected parties.

Second, the mandatory appointment of a *supervisor* monitoring the process can also be a desirable option in countries with a sophisticated body of insolvency practitioners, and only in the context of sales to unconnected parties. Moreover, creditors should still be entitled to challenge the transaction *ex post*.[133] In jurisdictions without a sophisticated body of insolvency practitioners, however, requiring the appointment of a supervisor can end up doing more harm than good. Therefore, in these countries, the sale of the company's assets should always be subject to *ex ante* approval from the creditors.[134]

Finally, regardless of the system of approval, there should be a comprehensive *disclosure regime*. If the transaction required *ex ante* approval, these disclosure obligations will allow creditors to make an informed decision. If the transaction can be challenged *ex post*, a detailed description of the transaction will facilitate investigations and, if applicable, the reversal of harmful transactions. Moreover, the existence of a comprehensive system of disclosure will reduce the risk of any opportunistic behaviour by debtors, buyers, supervisors, or any other relevant party.

7. Conclusion

This article has analysed the rise of pre-packs as a restructuring tool, the similarities and divergences in the use of pre-packs across jurisdictions, as well as the advantages and risks of pre-packs. It has been argued that, by shortening the length of insolvency proceedings, pre-packs have the ability to reduce the costs of financial

[132] Ralph (n 132). See also Luke Carney, 'Do the draft UK Pre-pack Regulations address industry concerns?', (National Law Review, 5 March 2021), accessible at <https://www.natlawreview.com/article/do-draft-uk-pre-pack-regulations-address-industry-concerns>. See also David Ampaw and Jared Green, 'The New Pre-pack Regulations – Controls on Transactions to Connected Parties' (DLA Piper, 14 April 2021) <https://www.dlapiper.com/en/uk/insights/publications/2020/11/the-new-pre-pack-regulations/> accessed 3 September 2021.

[133] See *Re Hellas Telecommunications* (n 49) at [8].

[134] Gurrea-Martinez, 'Insolvency Law in Emerging Markets' (n 101).

distress, especially those associated with the loss of reputation, employees, suppliers, consumers and goodwill. Thus, pre-packs can help maximise the value of the firm for the benefit of debtors, creditors and society as a whole. However, the conflicts of interests, lack of transparency and various forms of opportunistic behaviour potentially existing in pre-packs have raised some concerns about the desirability of this restructuring tool. After analysing the theory and evidence on pre-packs, this article has concluded by discussing whether countries should promote the use of pre-packs and, if so, how this mechanism can be adopted to serve as an efficient restructuring tool while providing effective protection to creditors.