

# High Court lends support to Pre-Pack Administration sales

December 2008



Since the Enterprise Act 2002, recent research has shown a significant increase in the use of pre-pack insolvency sales. Indeed the Enterprise Act reforms, arguably, made it easier for pre-packs to be undertaken following the introduction of the streamlined system of “*out of court*” routes into administration.

Providing that the pre-pack sale achieves one of the legislative hierarchies of administration objectives and the appointed administrator acts in the interests of all company's creditors, then there should not be a problem. Indeed, we all know that pre-pack sales are particularly effective where the inherent goodwill value of the business is at risk of deterioration post-insolvency. For example following an insolvency, key staff could depart from the business and/or the reputation of the business could deteriorate rapidly. However, detractors argue that pre-packs are open to potential abuse, both by directors planning for insolvency and insolvency practitioners acting as “*advisor*”, “*organising administrator*” and “*appointed administrator*”.

The decision in *DKLL Solicitors v HMRC* does not resolve the tension outlined above, but it does illustrate that the courts continue to be reticent to interfere with the commercial judgement of the appointed insolvency practitioner.

## Facts

This case concerned an application for an administration order by two partners of DKLL Solicitors. HMRC was DKLL's majority creditor and, having already issued a winding up petition against DKLL, HMRC vigorously opposed the application for an administration order. The underlying objective of the administration was to preserve the inherent value of the business, which it was proposed to do via a pre-pack sale out of administration.

## Decision

Ultimately, the court decided that the administration order should be granted and, whilst clearly cognisant of the objections raised by the majority creditor (HMRC), the judge observed that the pre-pack sale appeared to be the only way of saving DKLL's employees and that the sale would enable the affairs of DKLL's clients to be administered with the minimum of disruption.

## Comment

The judge did not consider the pre-pack strategy to be unlawful and tacitly recognised its value as a rescue tool. In this regard, the court will often place great reliance on the professional opinion of an experienced, impartial insolvency practitioner. Furthermore, the opposition of a majority creditor to a proposed administration and/or a pre-pack sale may not be enough to defeat an administration application, especially when there are other more compelling factors in favour of the administration. The case is also interesting, in so far as the majority creditor highlighted that the granting of an administration order, allied to the proposed pre-pack sale, in effect, would nullify its voting power at the subsequent creditors meeting. However, the court, whilst again appreciative of this position, realised that even if the majority creditors opposed the administrators' proposals, it was open to the administrator to seek the leave of the court for his or her proposals to be approved anyway.

*Please note: The content of this article is for information purposes only and further advice should be sought from a professional advisor before any action is taken.*