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# **A Comparative Look at Pre-Packs in Selected Jurisdictions**

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## Acknowledgement

This timely and very interesting Special Report looks at “pre-packs” in various jurisdictions by asking very specific questions about the process involved and the concerns that are raised in getting these approved in practice.

The fundamental question that pre-packs seek to answer is how to protect, preserve and maximise value in a trading business when it is prejudicial for it to continue to trade following the opening of formal insolvency proceedings. Pre-packs answer that question by bringing forward certain elements of the process, although this can give rise to concerns being raised regarding a lack of transparency and a perceived loss of independence by officeholders. As the Report demonstrates, there is significant divergence in the approaches that have been taken in different jurisdictions to seek to address these issues.

INSOL International wishes to sincerely thank **Ben Jones, INSOL Fellow** (Simmons & Simmons LLP, UK) for leading this important project to which a number of colleagues around the world have contributed. INSOL International would also like to thank the various authors for their contribution to this Report, which we have no doubt the INSOL membership will find useful and informative.

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## GUERNSEY

### 1. What measures are available in your jurisdiction to allow struggling businesses to enter into a “pre-pack”?

Guernsey stands out against many offshore jurisdictions because it has a dedicated administration regime designed to facilitate corporate rescue. The procedure is broadly similar to that in the United Kingdom, albeit it has been simplified and tweaked to suit Guernsey’s finance industry. For example, the desire to remain “creditor friendly” has seen the administration moratorium limited to not affect the rights of secured creditors.

Part XXI of the Companies (Guernsey) Law 2008, as amended (the Companies Law) sets out the grounds and procedure for applying for an administration order. The application must be for the purpose of achieving either:

- the survival of the company and the whole or any part of its undertaking as a going concern; or
- a more advantageous realisation of the company’s assets than would be achieved on a winding-up.

An application must be made to the Royal Court, supported by an affidavit seeking an order that the company be placed into administration and setting out the reasons why it should be placed into administration, and the purpose for which it is made. The application can be made by, *inter alios*, the company itself, a director, member or creditor. There is no out-of-court method of commencement.

The court has discretion to grant the order if it is satisfied that the company does not satisfy, or is likely to become unable to satisfy, the solvency test (which requires both balance sheet and cash flow solvency) and if it is satisfied that the purpose can be achieved.

Once appointed, an administrator has wide ranging powers exercisable in pursuit of the statutory purpose and may seek directions from the court as required.

Understanding the procedure assists when examining the use / availability of pre-packs. The Companies Law itself makes no specific references to them nor is there any other directly applicable legislation.

However, the Royal Court has consistently shown itself willing to be flexible and commercial in managing insolvencies and has been willing to look to England and Wales and other jurisdictions for guidance as to its procedure. For example, in *Esquire Realty*

*Holdings Limited*<sup>1</sup> the then Bailiff, Sir Richard Collas, was asked to consider an application for an administration order where it was intended to facilitate a pre-packaged sale of the company's assets immediately on appointment.

**2. How do pre-packs work in practice in your jurisdiction? What are the advantages and disadvantages of pre-packs when compared with other options that are available?**

Guernsey has few practical examples of pre-packs at work, but the considerations will be similar to those in England and Wales with a couple of notable differences.

The necessity of a court application will naturally increase the costs and possibly the time involved in securing appointments. Consequently, the procedure is less likely to be used for smaller scale local trading businesses (albeit doing so should not be impossible).

The process will require the proposed appointees to prepare a SIP 16-style report (see England and Wales) and so they must have the requisite expertise to do so.

**3. What duties must directors of the debtor consider when deciding whether to proceed with a pre-pack?**

Once the directors of a company become aware of the possibility that the company may fail the solvency test, their duties will be to act in the best interests of the company to maximise value in the company for the benefit of creditors as a whole, which includes future, as well as present, creditors. Those duties have equal application to a decision to proceed with an application for an administration order involving a pre-packaged sale albeit the level of court involvement (as set out below) may provide some comfort to directors that their decision-making will have had prior scrutiny by the court if they are later criticised.

Once the directors of a company become aware that it is unlikely to remain solvent, they will, in discharging their fiduciary duty to act in the best interests of the company by maximising its value, need to have regard predominantly to the interests of the company's creditors. The duty is still owed to the company itself, and not the creditors. This becomes more apparent when assessed against the test of wrongful trading in Guernsey which broadly mirrors the English position.

Directors need always bear in mind that the Royal Court has the capacity to adjust what are called "antecedent transactions" under the preference and wrongful trading provisions of the Companies Law. Hence, a train of authorities states that where a company was insolvent, the directors had to consider the interests of the creditors as paramount and take those interests into account when carrying out their duties to the company; and such duties may have also applied when the company was of doubtful solvency or on the verge of insolvency.

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<sup>1</sup> (17.04.2014) Royal Court (unreported).

Where a company is close to insolvency or the prospect of it seems genuine, the directors should operate on the basis that their decision-making may be scrutinised later if they did not give sufficient regard to how their decision-making would affect creditors. Consequently, careful minute-taking to support decisions and taking appropriate professional advice are steps that all boards should take.

#### 4. What level of involvement does a court have in a pre-pack?

The Royal Court has a very significant role in the pre-pack process because all applications for administration orders in Guernsey are heard by it.

In the *Esquire* case, the court was presented with an agreed proposal, endorsed by the intended administrators, that the business and its assets would be immediately sold to a newco upon the granting of an administration order. In exercising its discretion to grant the administration orders sought, the Royal Court concluded that it did not expressly approve the detailed arrangements of the proposed sale, but these were a material factor in the court's considerations and ultimately in the exercise of its discretion.

Notably, the Bailiff referred to the special risks of "pre-packs" as considered by the Royal Court of Jersey in *In the Matter of the Representation of Collections Group*<sup>2</sup> and considered guidance from the English High Court in *Kayley Vending Ltd*<sup>3</sup> and the decision of Kitchen J in *Halliwells LLP*.<sup>4</sup>

Importantly, the Bailiff endorsed the position held in the English High Court case *DKLL Solicitors v HMRC*<sup>5</sup> in which the judge held that the court, in exercising its discretion, may consider the interests of other stakeholders of the company. In *Esquire*, stakeholders included employees of the group and those for whom the group provided services (around 5,000 staff and 3,200 service users in 128 facilities together with close family members).

The Bailiff placed significant weight on the draft SIP 16 Report produced by the proposed administrators in accordance with the English and Welsh regime. That report considered the position of all creditors including those who would not benefit from the proposed arrangements. The Bailiff noted that, whilst there is no statutory requirement for a SIP 16 Report in Guernsey, it was of great assistance to the court and recommended that such report be produced in any similar applications.

As a result, the court plays a definitive role in the success of pre-packs in Guernsey. The application for the appointment of administrators will, by the nature of the procedure, require that details of the agreed sale are given in sufficient detail to allow the Court to

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<sup>2</sup> [2013] JRC 096.

<sup>3</sup> [2009] EWHC 904.

<sup>4</sup> [2010] EWHC 2036.

<sup>5</sup> [2007] EWHC 2067(Ch).

consider the proposal in the exercise of its discretion as to whether to make the appointment. A SIP 16-style report is, in practice, a pre-requisite.

**5. What duties must officeholders comply with when deciding whether to enter into a pre-pack?**

See question 1 above.

**6. How does the officeholder comply with their duties in practice? Can they rely on valuations? If so, what is regarded as an acceptable methodology?**

Again, see question 1 above. There is limited case law in Guernsey involving pre-packs. However, it is common practice for more than one administrator to be appointed joint administrators of Guernsey companies, with one typically being based in Guernsey and another based in the United Kingdom. For example, in the Esquire case, the joint appointees were both Guernsey and United Kingdom based. The practical experience of those overseas joint appointees will be highly relevant in any Guernsey appointment, particularly given the level of guidance taken by the Royal Court from English case law and procedure.

**7. What measures, if any, have been taken or are proposed to be taken to ensure that pre-packs are properly scrutinised?**

See above regarding level of court involvement. There is no specific regime for the scrutiny of pre-packs after the event.



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