Analysis of the corporate rescue procedures in the Insolvency Law of the UK and Cyprus: An empirical perspective

by Sofia Ellina

A thesis submitted to Lancaster University for the degree of Doctor of Philosophy in the Faculty of Arts and Social Sciences

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Abstract

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Administration and company voluntary arrangements can be used by economically distressed companies in the United Kingdom (UK) as rescue tools within its insolvency regime. In Cyprus insolvent companies have three legal options that operate as alternatives to liquidation: receivership, schemes of arrangement, and examinership. Through comparing but also taking a separate contextual analysis of the rescue procedures of the UK and Cyprus, this thesis examines these corporate rescue regimes and makes recommendations for their improvement. The efficiency of corporate rescue tools is assessed through an empirical research that includes quantitative data collection of administration and conduct of interviews in both the UK and Cyprus.

In May 2015, the Parliament of Cyprus made amendments to its insolvency law, which had the purpose of modernising the system and promoting a rescue culture. Companies Law (CAP. 113) was amended through the Insolvency Law 2015 N. 65(I)/2015, that included examinership. Receivership and schemes of arrangement pre-existed but examinership was implemented in the legislation after the amendment of CAP. 113 in 2015. Administration and examinership both have a primary common objective, which is to save the company, but their differences are significant as will be illustrated.

A key aim of this project is to evaluate Cyprus's current position and options in relation to corporate rescue with the influence of the efficacy of corporate rescue mechanisms in the UK and other jurisdictions.

On the whole this thesis will identify several aspects that need to be reconsidered for the UK corporate rescue regime to become more effective such as promoting a better treatment for creditors but at the same time enhancing rescue and an infrastructure to attract rescue finance as well as to minimise the disadvantages that arise from the contemporary practices. The lessons learnt from the UK will be used as an advantage to the Cypriot legislator. The Cypriot corporate rescue regime could become more appealing and ease access into the world of restructuring competitiveness, but certain caveats that will be highlighted could possibly obstruct this.

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Chapter 1 – Introduction

1.1 Overview and the Correlation between the UK and Cypriot insolvency rescue regime

Several jurisdictions have been preoccupied with the objective of identifying an insolvency rescue regime that would provide the ideal rescue outcome. Corporate rescue, however, has miscellaneous shades of interpretation which has given rise to debates amongst judges, academics and policy makers on the optimum rescue regime.[1] The issue of corporate rescue is crucial to countries with an established or emerging insolvency regime as it furthers their competitiveness in the global economic market. The constant development of commercial markets and the use of companies in that respect suggest that more effective means of pursuing rescue should be established.[2] The encouragement of entrepreneurs to take risks, giving a second chance to failing companies, keeping the employees unaffected and ensuring that the creditors will not be disadvantaged are the core pursuits of various legislators. The extensive leeway to the debtors could result in incentivising firms to take out debts irresponsibly, and the extensive creditor focus could also produce negative outcomes. Therefore, the virtuous approach is to balance the interests of stakeholders.

While the rescue culture was introduced in the United Kingdom (UK) under the Insolvency Act 1986 (IA 1986), this concept was not introduced in Cyprus until the enforcement of the Insolvency Law 2015 N. 65(I)/2015. The UK regime provides various alternatives that could aid struggling companies, but none of those procedures are overly focused on company rescue. The company survival is an onerous task,

[1] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (EE Publishing 2016) 4.
[2] Alice Belcher, *Corporate Rescue* (Sweet & Maxwell 1997) 11.

especially in the current economic climate, is a rationale for this approach.[3] The challenge of this thesis would be to identify the appropriate measures that could be imitated in the Cypriot insolvency framework in the light of the developments of the UK insolvency framework. An analysis of the rescue regimes of other jurisdictions such as the United States of America (USA) and Ireland will advance the analysis and enhance the recommendations of this thesis.

An ideal rescue procedure would not merely save the company in the short-term but ensure the long-term viability of the company.[4] Empirical studies have shown that rescuing the company is not a common result.[5] This insolvency outcome ('company rescue'), in comparison to the outcome of rescuing the company's business ('business rescue'), is evaluated.[6] Arguably, a viable company which is a going concern but has financial problems, could undergo a rescue procedure – even in insolvency – but a vastly financially damaged company should be liquidated. It is further argued that liquidation is not necessarily negative since this could lead to a creative destruction.[7] A salient consideration is that stakeholders often have differing interests during rescue; usually shareholders or employees have a different attitude towards company rescue than creditors or managers.[8] Their actions and the control that they are given could affect the outcome of a rescue process.[9]

[3] A contemporary example of failed rescue is *Re SHB Realisations Ltd (formerly BHS Ltd) (in Liquidation), Wright v. Prudential Assurance Co Ltd* [2018] EWHC 402 (Ch); [2018] BCC 712.
[4] See more about this in Chapter 2, Section 2.3.1.
[5] Sandra Frisby, 'Interim Report to the Insolvency Service on Returns to Creditors from Pre- and Post-Enterprise Act Insolvency Procedures' (July 2007); Alan Katz, Michael Mumford, 'Study of administration cases' (2007) 20 20 Insolv. Int. 97-103.
[6] Chapter 2 focuses on the difference between company and business rescue.
[7] See more in Chapter 2, Section 2.3.2.
[8] Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 197-198.
[9] See more about the main players of rescue in Chapter 2, Section 2.4.2.

The introduction of administration and company voluntary arrangements (CVAs) happened via the IA 1986 after the Cork Committee 1982.[10] Amendments to these rescue procedures were undertaken through the Insolvency Act 2000 and the Enterprise Act 2002 (EA 2002). This thesis examines in some detail these procedures. There have been numerous consultations/reports about ameliorating the regime; these works also endeavoured to identify provisions that would promote the ideal of collectivity[11] in an insolvency scenario.[12] Some elements of administration that are scrutinised through this thesis are the hierarchical objectives,[13] the moratorium,[14] pre-packaged administration,[15] rescue funding[16] and the exit routes.[17] Albeit football clubs, high street retailers and restauranteurs utilise CVAs, it seems that the figures in other business sectors are disappointing.

The Cypriot legal system contains English cases and legislation due to residues from the British Empire. After the grave banking crisis of 2013 in Cyprus,[18] it was

[10] Chapter 3 focuses on CVAs and Chapter 4 on Administrations.
[11] Collectivity does not mean the equality of stakeholders but balancing their interests. See *Re Smith, Knight & Co; ex p. Ashbury* (1868) LR 5 Eq 233.
[12] Department of Trade and Industry (DTI) White Paper, *Our Competitive Future: Building the Knowledge Driven Economy* (Cm 4176, December 1998); The Insolvency Service, A Review of Company Rescue and Business Reconstruction Mechanisms (London HMSO, 1999); Insolvency Service, A Review of Company Rescue and Business Reconstruction Mechanisms, Report by the Review Group (DTI, 2000); DTI/Insolvency Service White Paper, *Productivity and Enterprise 'Insolvency – A Second Chance* (Cm 5234, 2001); The Insolvency Service, Encouraging Company Rescue – a consultation, (June 2009); The Insolvency Service, Consultation/Call for evidence Improving the transparency of, and confidence in, pre-packaged sales in administrations, (March 2010); The Insolvency Service, Proposals for a Restructuring Moratorium - a consultation, (July 2010); The Insolvency Service, A Review of the Corporate Insolvency Framework: A consultation on options for reform the Corporate Insolvency Framework response form (25 May 2016) (2016 Consultation); Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) (ICG Report 2018).
[13] See Chapter 4, Section 4.2; IA 1986, Sch B1, para 3.
[14] See Chapter 4, Section 4.6; *Bristol Airport v. Powdrill* [1990] Ch. 744.
[15] See Chapter 4, Section 4.5.
[16] See Chapter 4, Section 4.7.
[17] See Chapter 4, Section 4.6; HM Revenue & Customs 'Exit routes from administration' archived on 7 February 2014 <https://webarchive.nationalarchives.gov.uk/20140207024320/http://www.hmrc.gov.uk/manuals/insmanual/INS3217.htm> accessed 13 September 2019.
[18] Patrick Baz, 'Final 'haircut': Cyprus to levy deposits by 47.5 percent' 26 July 2013 <https://www.rt.com/business/cyprus-crisis-bailout-deposit-631/> accessed 03 November 2019.

essential to impose strict and effective measures that would alleviate companies from the difficulties. This also had as a purpose the progression of the economy. The Cypriot legislator, therefore, in 2015 introduced an insolvency regime that is archetypal to the Irish Insolvency Law. Cypriot Companies buried in economic hardship have three legal options which are alternatives to liquidation: receivership;[19] schemes of arrangement;[20] and examinership.[21] The Cypriot schemes of arrangement are modelled after the English Companies Act 1948 schemes of arrangement but some changes took effect in 2015.[22] Receivership and schemes of arrangement pre-dated the 2015 reforms. The only process in Cyprus that directly has the purpose of rescuing the company is examinership. Financially ailing companies though tend to choose alternative mechanisms such as receivership.[23] Some significant variations distinguish the Cypriot examinership from the UK administration, although they were characterised as equivalent.[24] This thesis underpins that their impact and effectiveness deviates in several instances.[25] The legal influences of the UK towards Cyprus as well as the prominence of the insolvency rules of the UK universally, incentivised the initiation of this comparison. It is assumed that the Cypriot legislator could learn from the merits and drawbacks of the UK insolvency regime.

[19] See Chapter 5, Section 5.3.
[20] See Chapter 5, Section 5.4.
[21] See Chapter 5, Section 5.5.
[22] See Chapter 5, Section 5.4.1.
[23] See Chapter 5, Section 5.5.2.
[24] David Stokes, 'Cyprus: insolvency - law reform' (2015) 30 J.I.B.L.R. N126; Maria Kyriacou, 'Bolder and Better?' Recovery (Autumn 2015) 29; Elias Neocleous, 'Cyprus: insolvency – reform' (2015) 26 I.C.C.L.R. N85.
[25] See Chapter 5, Section 5.6.

1.2 Jurisdictional comparison and the EU approach

This thesis highlights aspects of the USA Chapter 11 and the Irish examinership, that could strengthen the current corporate rescue procedure in the UK and Cyprus. Emphasis is given on characteristics that could be less functional and on recommendations regarding legal transplants. These jurisdictional comparators were selected because Chapter 11 in the US Bankruptcy Code 1978 is regarded as a leading restructuring mechanism globally[26] since many jurisdictions used Chapter 11 – including examinership in Ireland – as an exemplary for implementing their own mechanism.[27] Examinership in Ireland has been in force since 1990[28] thus it would be vital to elucidate the aspects that deviate from the Cypriot examinership. The purpose is to ameliorate the Cypriot examinership and/or suggest an alternative rescue process with the aim of persuading companies to embrace rescue attitudes within the society. The USA Chapter 11 must be observed since one of its key characteristics is that it supposedly has a debtor-friendly approach[29] as opposed to the law in the UK, which is described as pro-creditor.[30] Still, some would argue that EA 2002 reform is transforming the UK approach to pro-debtor in lieu of pro-creditor,[31] whereas the USA is gradually turning into pro-creditor by taking into consideration the cram down on creditors and the strong role of creditors in the debtor-in-possession (DIP) insolvencies.[32] Cyprus, before the 2015 inclusion of the insolvency framework into the

[26] As per the World Bank Doing Business Rankings on resolving insolvency, the USA 2nd in ranking. For the global rankings see <https://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency/score> accessed 19 February 2020.
[27] Gerard McCormack, 'Corporate restructuring law - a second chance for Europe?' (2017) 42 E.L. Rev. 532-561; Muir Hunter, 'The nature and functions of a rescue culture' (1999) J.B.L. 520.
[28] Companies (Amendment) Act 1990 and now Companies Act 2014 (CA 2014).
[29] See Chapter 6, Section 6.2.2.1.
[30] Sefa Franken, 'Creditor- and debtor-oriented corporate bankruptcy regimes revisited' (2004) 5 E.B.O.R. 645-676.
[31] Gerard McCormack, 'Super-priority new financing and corporate rescue' [2007] J.B.L. 701-732.
[32] David Skeel, 'Creditors' Ball: The "New" New Corporate Governance in Chapter 11' (2003) 152 University of Pennsylvania Law Review 917.

legislation, had a creditor-oriented approach. Examinership is a process that is more debtor-oriented hence, the question is whether this process can survive in an environment that has always been creditor-oriented.[33]

The legislative similarities between the UK and Cyprus are apparent and simultaneously their backgrounds diverge. The social and economic backgrounds of these countries probably affect their different rescue attitudes. The UK introduced a rescue attitude more than 30 years ago after the Cork Report, whereas the Cypriot legislator attempted to take that orientation approximately 5 years ago. The necessity of acclimatising with the synchronous European countries led Cyprus to orchestrate a process that is more rescue oriented rather than adhering to a process that is focussed on asset realisation. The European Commission on 22 November 2016 initiated a proposal for a draft Directive on restructuring as the importance of taking rescue agenda is now acute.[34] The UK sought for a national reinvigoration through the recent consultations of 2016 and 2018, which were conceivably a response to the Directive proposal.[35] This Directive that targets early restructuring and entrepreneurship encouragement was officially implemented in June 2019.[36] This directive is arguably an answer to Chapter 11[37] thus, the directive references as well as the analysis of the most significant features of Chapter 11 are inevitable. The UK already has a reform agenda with the August 2018 proposals that take steps towards the USA Chapter 11. This signifies that even after the exit of the UK from the European Union (Brexit) the

[33] See Chapter 5, Section 5.5.2; Andri Antoniou, 'Examinership: A Missed opportunity' CRI Group, 24 October 2018 <http://www.crigroup.com.cy/wp-content/uploads/2018/10/Examinership-A-missed-opportunity.pdf> accessed 14 October 2019; Kayode Akintola, Sofia Ellina, 'The Use and Abuse of Corporate Insolvency Rescue Procedures: A Contextual Evaluation of the United Kingdom and Cyprus' in Jennifer L. L. Gant (ed), *Party Autonomy and Third-Party Protection in Insolvency Law* (INSOL Europe 2019) ISBN 978-0-9931897-7-7, 137-154.
[34] COM(2016) 723 final 2016/0359 (COD).
[35] 2016 Consultation (n 12); ICG Report 2018 (n 12).
[36] Directive (EU) 2019/1023 (the 2019 directive).
[37] McCormack, 'Corporate restructuring' (n 27).

UK is still seeking to remain competitive in the global market of restructuring. The UK legislators might decide to implement the provisions of the directive with the aim of conceivably remaining one of the competitor countries within Europe and internationally. The background circumstances of each country are mentioned throughout the thesis in order to be able to point out the reason(s) for success, failures as well as similarities and differences.

1.3 Research Question(s)

The main research question of this thesis is to generate ideas and suggestions about the amelioration of the Cypriot corporate rescue regime that are endeavoured through the assessment of the UK corporate rescue regime. Through addressing further subsidiary questions, the conclusions of this research could be strengthened. The evaluation of the juxtaposition between company and business rescue turned out to be crucial for discovering the optimum rescue regime. The identification of the impediments and virtues of CVAs and administrations could operate as precepts of avoidance for the Cypriot legislator. In other words, this thesis highlights several recommendations that can conceivably enhance the current Cypriot legislation regarding rescue/restructuring in the light of the administration and CVA developments in the UK. The qualitative and quantitative data collection[38] that was conducted for the purposes of this thesis is tied into the subsidiary research question on the value of administration as a rescue tool and feed into arguments on whether corporate or business rescue should be pursued.

This research is not only scrutinising the available rescue/restructuring mechanisms in Cyprus but also whether the rescue processes features that are available

[38] Discussed in Chapter 1, Section 1.5.

in the UK can be compatible with the Cypriot background. The discovery of whether administration could have been a better fit than examinership in Cyprus seems imperative as well as exploring the other available processes that are alternatives to liquidation. This introduces a further comparative perspective to the research question, using jurisdictions such as the USA and Ireland as comparators to explore the possibility of recommending legal transplants for the UK and Cypriot rescue culture.

The lack of company cash-flow could diminish any rescue prospects. Therefore, a key aspect for answering the research question is through determining the availability of financing sources for distressed companies. Incentives and devices that are used in the UK and the USA give rise to a fundamental analysis. DIP financing is considered as an effective device that increases the chances of company rehabilitation.[39] This gives justice to the inclusion of USA Chapter 11 as an additional jurisdictional comparator. The exploitation of a procedure for different means rather than its purpose can damage the trustworthiness and accountability of an insolvency regime. Thus, various investigations of this thesis regarding the UK and Cypriot mechanisms will have as an aim the mitigation of future harms. The actual rescue procedure might not be that problematic but the aftermath of it could be. Issues that arise from the nature of the rules and the necessary persuasions that surround these cultures are scrutinised.

1.4 Objective and contribution of the research

The purpose of this research is to provide a legal analysis of the ways a rescue culture in insolvency law can develop and function in the UK and Cyprus. The initiation of the insolvency regime and especially of examinership is a novel action and at a primary

[39] Analysis in Chapter 6, Section 6.2.3.

stage in Cyprus. The Cypriot examinership is modelled after the Irish examinership but, as highlighted further, the effect in each country is different. The low probabilities of achieving a lasting company rescue acted as a crucial incentive that led to the conduct of further research on improving these mechanisms.

This project can be considered as unique since this comparison was previously non-existent and the literature review of this area is still in its infancy in Cyprus. The empirical dimension is also original as it provides new/additional data to pre-existing empirical works on insolvency outcomes. The qualitative and quantitative data collection methods that were conducted for this thesis have as a purpose to empirically discover the gaps of the legislation and make amendment recommendations for both the UK and Cyprus.[40] As an infrastructure of an effective corporate rescue regime could contribute to the economic development – although macroeconomic factors could affect this – the identification of advantageous changes to the mechanism could benefit both countries, through its publication.

The ideal outcome might be to some the survival of the company. Whether or not this is ideal could depend – to an extent – on its impact on stakeholders. The survival of the whole company is also more arduous than saving the business or part of it. The full or partial business rescue happens when the activities of the company continue but possibly under a different authority.

Examinership was introduced to the Cypriot legislation as the main rescue procedure in 2015 but receivership is currently more prevalent. Although, it is still premature to form an opinion about the success of examinership, the perception that examinership is insufficient for aiding companies in Cyprus has appeared.[41] Another

[40] For more information about the methodology of this thesis see Chapter 1, Section 1.5.
[41] See Chapter 5, Section 5.5.2.

issue is that Insolvency Practitioners (IPs) struggle to use examinership due to its obscure outcome. Indeed, one might expect IPs to encounter teething problems associated with the familiarity to receivership and aversion to change. This generates an interest in assessing whether Cyprus has a compatible infrastructure for implementing examinership to the insolvency regime.

Creditors of struggling companies in Cyprus usually use receivership as an alternative to liquidation. Receivership can achieve one or both of two aims: to realise company assets to obtain a better return to the secured creditor; and a business sale through a trading receivership.[42] Cyprus's insolvency framework was modelled after the Irish framework but the UK also had major influences. The rules of receivership are found in the Cypriot Companies Law, Chapter 113 (CAP. 113) which is modelled after the Companies Act 1948 therefore, receivership is akin to the receivership used before the implementation of IA 1986. Post-2015 amendments in Cyprus made it compulsory to have an IP acting as a receiver. Cyprus has a limited number of decisions concerning receivership therefore, the UK precedent is frequently applied in Cypriot courts.[43] The UK administrative receivership (AR) is a controversial procedure that influences a lot of debates around it; one group of people says that it always resulted in the liquidation of the company, but another group argues that AR is misconceived since it operated as a rescue instrument for the business, specifically by hiving down.[44]

[42] See Chapter 5, Section 5.3.1.
[43] *Bank of Cyprus Public Company Ltd v. Orphanides Public Company Ltd* (2014) District Court of Larnaca, Application number: 4221/2013; *Panas Hotels Ltd and others v. Astrobank Limited and others* (2017) District Court of Famagusta, Application number: 343/2017; *Optikos Oikos Theophanides Ltd and others v. Bank of Cyprus and others* (2018), District Court of Nicosia, Application Number: 782/2018.
[44] See Chapter 4, Section 4.5.3.

In pro-creditor regimes, companies are less likely to be purely rescued than in pro-debtor regimes.[45] Rescue procedures are typically funded by taking security over current assets but there are questions on the funding regime and monitoring by secured creditors.[46] This leads to the query whether the rescue procedures are working efficiently in the UK as regards to balancing the interests of stakeholders. The investigation as to which is the ultimate rescue mechanism is complex and not straightforward, since a process that is effective in the UK might not have the same aftermath in other jurisdictions. This research does not only target to impact the academic community but also professionals such as banks, lawyers, accountants and legislators.

1.5 How does the research methodology contribute towards answering the research question of this thesis?

This thesis seeks to explore the effectiveness of administration and CVAs, where this analysis will act as an exemplar for achieving progress in Cyprus regarding corporate rescue. This examination is conducted through using an empirical and a doctrinal research but also through other methodological ideas such as Darwinian theory,[47] utilitarianism[48] and jurisprudence. Therefore, these theories/ideas that have been applied as well as the empirical findings aided to undertake pragmatic legal considerations. The justifications of the arguments also rely on comparative approaches as well as considering legal transplants.

[45] See Chapter 6, Section 6.2.2.2; Ron Harmer, 'Comparison of Trends In National Law: The Pacific Rim' (1997) 23 Brook.J.Int'lL.146, 147-148.
[46] Louise Gullifer, Jennifer Payne, *Corporate Finance Law: Principles and Policy* (2nd edn, Hart Publishing 2015) 306.
[47] See Chapter 2, Section 2.3.2, page 30.
[48] See Chapter 4, Section 4.4, page 106 and Chapter 6, Section 6.2.2, pages 213, 214 and 256.

This thesis contains two empirical methods: quantitative and qualitative data analysis. Since the most essential act before initiating an empirical research is to attain the approval of the university ethics committee, an application for ethical approval was submitted on 7th December 2016. The application was accepted on 23rd March 2017, and the empirical data collection started in the beginning of 2018. These methods facilitate an evaluation regarding the efficiency of corporate rescue models in the UK and Cyprus. All chapters contain aspects from the empirical research. The quantitative data analysis can be found mainly in chapters 2 and 4 but there have been referrals to some results from the data for the purpose of proving a point in chapter 6. Excerpts from the interviewees that were conducted for the qualitative data analysis are included in all main chapters. This research also embraces a comparative approach which is administered through doctrinal research. This helped to shed light on the quantitative and qualitative data.

The quantitative data collection contains a compilation of information through the random selection of 600 insolvent companies that entered administration in England and Wales between 2012-2016, that are available to the public via Companies House. One of the impediments of this research was that a quantitative data analysis of the companies that went into examinership or receivership in Cyprus was unattainable. This is because the insolvency documents are not published online, which means that anyone who wants to investigate a company file must physically go to the Registrar of Companies to request for that file. This company search is followed by a fee of €10 per company. Despite this, there is another constraint as regards to examinership since there have only been a handful of cases, which could not have produced statistical significance.

The companies were firstly identified in the Gazette that has an index of insolvency appointments.[49] The necessary documents were downloaded from the Companies House website[50] to enable the extraction of information. These documents include the following: notices of appointment of the administrator, statement of affairs, administrator's progress reports, administration extension notices, notices of disclaimer under section 178 of the IA 1986, liquidator's progress reports and notices of dissolutions. The extracted information was initially added to Microsoft Access and then exported to Microsoft Excel to illustrate the results of the analysis through graphs.

The database has several information that includes the following: date of incorporation; date of administration; administrator's appointor; administration objective; floating charge's presence; date of floating charge; companies that undertook factoring and invoice discounting agreements; identification of other security; secured debt and return; preferential debt and return; unsecured debt and return; identification of pre-administration CVA or administration; floating charge realisation; prescribed part's presence; prescribed part's cost; amount received from prescribed part; value of floating charge; value of prescribed part; expenses of administration and remuneration of the administrator incurred; paid expenses of administration and of the remuneration of the administrator; outcome of administration; the presence of pre-packaged administrations; administration exits route; Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE) transfers; and a notes section. Some of the statistical findings are also demonstrated through graphs, and several variables are cross-referenced to have a more elaborate analysis.

[49] The Gazette: Official Public Record <https://www.thegazette.co.uk/insolvency> accessed 04 November 2019.
[50] Companies House < https://beta.companieshouse.gov.uk/> accessed 04 November 2019.

Qualitative data collection is the second method, which involves the use of semi-structured interviews to deepen understanding of certain facets of the quantitative data, and to extract new information.[51] This research includes 9 interviewees in England and Cyprus who received a participation information sheet[52] and a consent form[53] via email before they agreed to officially participate. The process was done in accordance with the participation information sheet, which states that all personal information about the interviewee will be kept confidential. Interviews were audio recorded and transcribed for the convenient compilation of the material. These audio recordings were anonymised along with hard copies of any data. The audio recordings will be erased once this research is completed. The interviewees are referenced in accordance with OSCOLA, subject to the need of preserving anonymity. The interviewees are IPs, lawyers, an academic and a credit manager. More details about all the interviewees can be found in Appendix D. All interviewees have years of experience in insolvency thus, their contribution to the research was invaluable. Some of their views are contradicting therefore, it is interesting to depict their rationale through the justification of their arguments. The information that was retrieved from the Cypriot interviewees was paramount since the literature in Cyprus is limited.

A crucial aspect of the empirical research is to pinpoint the insolvency outcomes: corporate rescue, business rescue (including pre-packaged administration) and creditor distribution. Other valuable points that came to light from this exercise are the determination of the lifespan of the distressed company, the administration expenses/fees returns, and the evaluation of the prescribed part. Aspects that rose from this quantitative analysis led to some subsidiary research questions, that led to the need

[51] The list of questions is attached as Appendix A.
[52] Attached as Appendix B.
[53] Attached as Appendix C.

of discovering the handling of practical issues. Thus, the interviews were an imperative dimension for this thesis.

It was intelligible that a key to this research was the combination of various research methods. If this thesis merely relied on a doctrinal methodology, various legal aspects would not have been considered. The most rationalistic approach as regards to the research methodology was not to rely only on the empirical data either, since there were clearly some limitations. These constraints include *inter alia*, sample size, personal/professional bias, incomplete or inaccurate information in filed reports.

1.6 The structure of the thesis

The thesis contains seven chapters. Following this introductory chapter, the second chapter will focus on distinguishing corporate rescue from business rescue with references to the UK rescue procedures. As the UK is a main comparator of this thesis, this chapter focuses on how corporate rescue is perceived in the UK. This chapter determines whether company failure could provoke any advantages and the lifespan of companies is compared to the rescue outcomes. This happens with the aim of developing an understanding about the importance of rescue. Company rescue is compared to business rescue with a discussion that is reinforced by the quantitative and qualitative data analysis of this thesis. The investigations of this chapter also include the perspective of the main stakeholders about rescue and highlights their impact towards rescue.

Chapter 3 continues with an assessment of the rationale behind the unattractiveness of CVAs and explores the prominent attention that large retail companies have given to CVAs. This necessitates an analysis about the utilisation,

limitations and strengths of CVAs. This chapter identifies the reasons that SMEs do not prefer CVAs and examines whether the rejuvenation of this mechanism is necessary. The treatment of landlords is considered for some of the conclusions of this thesis. The views of interviewees about the aforementioned issues give a further element to the discussions.

Chapter 4 examines administration – which is the dominant rescue procedure in the UK – in terms of effectiveness and solutions are suggested that target to mitigate its challenges. The discussions focus on prevalent matters of administration such as pre-packaged administration, rescue funding, the effect of Brexit and various aspects of the moratorium. The empirical evaluation provides results regarding the appointor of the administrator, the administration objective, the outcome of administration, the debts and returns to secured, preferential and unsecured creditors, the administration exit, and expenses/remuneration incurred and paid to IPs. Some of these results are compared for making further deductions. Also, insolvency experts reveal their concerns and arguments, that are used for the enhancement of the thesis analysis.

Chapter 5 takes a historical retrospection of the Cypriot insolvency background and discovers the problems of the Cypriot receivership, schemes of arrangement and examinership. Solutions that could mitigate the extent of the problems and provide a more effective corporate rescue framework are emphasised. The acumens of insolvency experts in Cyprus are provided as justifications for a variety of arguments that are discussed in this chapter.

Chapter 6 focuses on Chapter 11 bankruptcy in the USA, which bears the debtor-in-possession feature and provides super-priority creditors. The effectiveness of these characteristics and whether they could succeed in either the UK or Cyprus are determined. The Irish examinership is considered as a successful rescue procedure

hence, it is vital to discover the strengths of the Irish examinership and what makes it different from the Cypriot examinership.

Chapter 7 concludes the thesis. It provides a synopsis of the arguments contained in the thesis. Finally, the conclusion identifies further research prospects that could arise from this thesis and ideas for reforms are put forward.

Chapter 2 – Company Rescue versus Business Rescue

2.1 Introduction

Most jurisdictions across the globe – whether common law or civil law influenced – include corporate rescue procedures into their legislation and there is an accentuated persistence in the area. Therefore, an exegesis on what constitutes a successful corporate rescue regime is crucial. The legislators of these countries are in search for an ideal solution that would create an environment in which a company could come out of its financial difficulties. Legislators in several jurisdictions direct their main focus in terms of reform towards corporate rescue.[1] A crucial deliberation is whether the company survival is a realistic outcome and whether business rescue could generate a more beneficial outcome for the stakeholders.

Rescue should be emboldened before the company encounters major financial difficulties since a prevalent problem is that measures to circumvent insolvency are not undertaken, which could lead to the infeasibility of the survival. Company rescue is the total rescue of the entity which is characterised as 'pure rescue'.[2] Strictly speaking, company rescue cannot be characterised as pure rescue since the company loses/removes a non-profitable/problematic part of its business. Business rescue is the salvation of the business or part of the business of the company, which is sold to a new company (Newco). A business rescue can result in a corporate recycling and an asset sale. The previous owners of the business can also be the owners of the Newco, which is a reason that controversial criticisms are generated. When the same people are

[1] Bruce Carruthers, Terence Halliday, *Rescuing Business: The Making of Corporate Bankruptcy in England and the United States* (Clarendon Press 1998) 509.
[2] Sandra Frisby, 'In Search of a Rescue Regime: The Enterprise Act 2002' (2004) 67 M.L.R. 247-272, 248.

managing the company, the survival of the company could be in jeopardy.[3] As this is undermining business rescue, this chapter explores the benefits of business rescue and signalises the hurdles of facilitating company rescue. Graphs that were designed from the quantitative data extraction are utilised in this chapter, along with excerpts from insolvency experts that were interviewed for the purposes of this thesis.

Companies have to evolve with contemporary social and economic changes to prevent financial distress and/or insolvency.[4] The understanding of the factors that lead to company failure shed light on the discussions about the impact of company stakeholders towards company rescue. Since the United Kingdom (UK) is a main comparator of this research, this chapter mainly concentrates on the UK rescue perception. The Cork Committee captured and explained the idea of rescue culture in 1982.[5] The application of rescue culture within the legal culture of the UK has been a contentious matter. Lord Browne-Wilkinson officially approved and interpreted 'rescue culture' in *Powdrill v. Watson*[6]*(Powdrill)*. Further cases[7] as well as the UK government, bankers[8] and the legislation have endorsed rescue culture.[9] The Cypriot examinership emanates from the Irish examinership thus, it is essential to note that Part IX of the Companies Bill 1987 in Ireland that included examinership originates from the Cork Committee recommendations.[10] Since there was an attempt to tie the Cypriot framework

[3] Peter Walton, Chris Umfreville, 'Pre-Pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration' University of Wolverhampton (2014).
[4] Alice Belcher, *Corporate Rescue* (Sweet & Maxwell 1997) 11.
[5] Report of the Review Committee on Insolvency Law and Practice (Cmnd 8558, 1982) (Cork Report).
[6] [1995] 2 AC 394.
[7] *Thomas v. Ken Thomas Ltd* [2006] EWCA Civ 1505 by Neuberger LJ; *Re Farnborough-Aircraft.com Ltd* [2002] 2 BCLC 641 by Neuberger J; *Re Demaglass Holdings Ltd* [2001] 2 BCLC 633 by Neuberger J, *On Demand Information plc (in administrative receivership) and another v. Michael Gerson (Finance) plc and another* [2000] 4 All ER 734 by Robert Walker LJ.
[8] British Bankers Association, 'Banks and Businesses Working Together' (1997); Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 202.
[9] Enterprise Act 2002(EA 2002); Insolvency (Protection of Essential Supplies) Order 2015 SI 2015 No. 989.
[10] Irend Lynch, Jane Marshal, Rory O'Ferrall, *Corporate Insolvency and Rescue* (1st edn, Butterworths 1996) 261.

with rescue culture in 2015, the comprehension of the application of rescue culture in the UK, which a common law jurisdiction is vital.

2.2 The development of 'rescue culture'

An important aspect of rescue culture is the fact that it is a 'culture'. Cultures cannot be forced on jurisdictions, but they can merely evolve over time.[11] A historical backdrop highlights the development of rescue culture in the UK as well as to what extent it was achieved. The term 'rescue' has contradicting meanings thus, the following analysis also aims to the comprehension of the UK corporate rescue regime.[12]

While in the first half of the Victorian era[13] and prior to that period, the insolvency regime was draconian as the imprisonment of debtors was allowed, in 1869 imprisonment was abolished.[14] This led to a more indulgent approach towards failure where the creditors struggled to adapt.[15] Attempts to introduce a form of rescue can be traced back to debates of the Bankruptcy Bill in 1883 that were about personal insolvency. The President of the Board of Trade, Joseph Chamberlain, said "Parliament had to endeavour, as far as possible, to protect the salvage and also to diminish the number of wrecks".[16] Following this, the official receiver was created, with the Bankruptcy Act 1883, who was characterised as "the watchdog of the public".[17] The initiation of corporate rescue procedures do not only have the purpose of providing a

[11] David Brown, Corporate Rescue – Report for the Ministry of Economic Development (November 2000) <https://www.iiiglobal.org/sites/default/files/6-_corp_rescue.pdf> accessed 18 April 2019.
[12] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (EE Publishing 2016) 4.
[13] See more about Victorian insolvency: V Markham Lester, *Victorian Insolvency* (Clarendon Press 1995); E Welbourne, 'Bankruptcy Before the Era of Victorian Reform' (1932) Cambridge Historical Journal 51.
[14] John Tribe, 'The imprisonment for debt jurisdiction' (2018) 31 Insolv. Int. 92-100, 96.
[15] David Milman, David Mond, *Security and Corporate Rescue* (Hodgsons 1999) 53.
[16] Hansard, HC Deb (19 March 1883), Vol. 277 cc817.
[17] Muir Hunter 'The nature and functions of a rescue culture' [1999] J.B.L. 520.

second chance to struggling companies but also the persuasion of the soundness of companies.[18] Rescue culture carries a positive, protective, corrective and punitive role.[19] The Cork Committee believed that the initiation of these mechanisms also necessitated the incorporation of wrongful trading rules.[20] The main target was to generate incentives for directors to seek a solution at a preliminary stage.[21] When the director's action is delayed, this might mean the failure of the company as the company value can progressively deteriorate.[22] The attempt of the legislator to encourage rescue through the enforcement of wrongful trading rules was legitimate. Yet, wrongful trading rules force precipitate insolvencies due to the threat of personal liability of the director. Insolvency Practitioners (IPs) – who influence the decisions of directors – usually advise the directors that through filing for liquidation the stakeholders would be in a better position.

After the introduction of the Insolvency Act 1986 (IA 1986), there have been several reports that acceded into discouraging failure and invigorating rescue.[23] The initiation of these procedures anticipated the augmentation of rescue and simultaneously the prevention of company distress.[24] Company failure is not necessarily a negative thing though.[25] The Cork Committee reinforced this through insinuating that not all rescues are realisable.[26] The judiciary clarified that only viable enterprises with the prospect of being saved should be sustained.[27] When the prosperity of the entity and/or

[18] Belcher (n 4).
[19] Hunter (n 17).
[20] Cork Report (n 5) para 239.
[21] Carruthers and Halliday (n 1).
[22] David Milman, *Governance of Distressed Firms* (EE Publishing 2013) 18.
[23] White Paper, 'Our Competitive Future: Building the Knowledge Driven Economy' (DTI December 1998); The Insolvency Service, A Review of Company Rescue and Business Reconstruction Mechanisms (London HMSO, 1999).
[24] Sir Kenneth Cork, *Cork on Cork: Sir Kenneth Cork Takes Stock* (Macmillan 1988) Chapter 10.
[25] See Chapter 2, Section 2.3.2.
[26] Cork Report (n 5) paras 198 (j), 203, 204.
[27] *Powdrill* 442.

the enterprise is an indispensable part of the society of a region, a rescue attempt would be essential.[28]

The perception that the EA 2002 would enhance the rescue attitude was apparent. There was even an attempt to reiterate this through the legislation's nomenclature that referred to an 'enterprise' instead of an 'insolvency'. A minister in 2003 said that: "These new measures should help to promote a rescue culture and help more companies survive when they get into financial difficulties."[29] The enforcement of the EA 2002 was also characterised as "the further development of the rescue culture".[30] The evolution of administration to a collective procedure and the near elimination of administrative receivership (AR)[31] influenced these concepts. Although AR was abolished because it was not aligned with rescue,[32] Cork suggested that AR rescue is possible through hiving down.[33]

What is anticipated in the UK by the form of rescue culture is reasonably distinct than what is expected in other countries that could be characterised as more debtor-oriented.[34] As such, the UK rescue culture welcomes business sales as well as asset sales. This is acceptable only if it is demonstrated that this is the best possible outcome

[28] Cork Report (n 5) para 204.
[29] Heather Tomilson, 'Insolvency rule change boosts 'rescue culture'' Independent, 14 September 2003 <https://www.independent.co.uk/news/business/news/insolvency-rule-change-boosts-rescue-culture-579921.html> accessed 03 February 2019.
[30] Insolvency Service, A Review of Company Rescue and Business Reconstruction Mechanisms, Report by the Review Group (DTI, 2000) 9.
[31] The exceptions to the availability of AR can be found in IA 1986, s 72A-H.
[32] DTI/Insolvency Service White Paper, *Productivity and Enterprise 'Insolvency – A Second Chance* (Cm 5234, 2001).
[33] Cork (n 24); See more about AR in Chapter 4, Section 4.5.3 and Chapter 5, Section 5.6.
[34] For a comparison between creditor-oriented and debtor-oriented approaches see Chapter 6, Sections 6.2.2.1 and 6.2.2.2.

for creditors.[35] The company creditors and other stakeholders add a different input, that could affect the outcome of a rescue procedure.[36]

2.3 Why do companies fail and how does this affect rescue?

Naturally anything that is connected or interacts with the human existence could collapse.[37] Some company failures are inevitable and there are, in fact, internal and external factors that contribute to this collapse. Internal factors could include amongst other things, the poor corporate governance of the company and the lack of cash-flow. External factors can include negative market conditions and economic crises.[38] In essence, if the reasons that brought the company into financial difficulties are detected, the company might be able to overcome the problems and failure can be curtailed through raising awareness.

An endogenous issue that could lead the company into insolvency is the deficiency in cash thus, the cash-flow of a company can demonstrate whether the company is solvent or not.[39] A company is at a risk of failure if the balance sheet indicates a profit but there is no liquidity.[40] The cash-flow test and/or the balance sheet test can determine whether a company is insolvent. The company fate extensively depends on the directors who have to ensure that enough cash comes in the company

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[35] Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (EE Publishing 2008) 306.
[36] See Chapter 2, Section 2.4.2.
[37] Paul Ormerod, *Why Most Things Fail: Evolution, Extinction and Economics* (Faber & Faber 2005) Chapter 13.
[38] Bank of England, 'Financial Stability Report' October 2008, Issue No 24 <https://www.bankofengland.co.uk/-/media/boe/files/financial-stability-report/2008/october-2008.pdf?la=en&hash=DA2C19274CA14E7F6CAE953CEF3FD046B553265C> accessed 08 February 2019.
[39] Cash-flow test in IA 1986, s 123(1)(e).
[40] Balance sheet test in IA 1986, s 123(2).

accounts for covering the company's liabilities.[41] Planning must take place at an early stage to enable the avoidance of cash-flow problems.[42] Creditor consultation, programmes that would regulate costs, market development, product strategy and negotiation of credit lines need to be planned in advance. Cash-flow insolvent issues can be temporarily settled by borrowing that amount[43] or by realising some of the current assets.[44] This would only be a short-term solution for the company though. *BNY Corporate Trustee Services Ltd v. Eurosail-UK 2007-3BL Plc*[45] highlights the caution about these tests.

The above problem is directly associated with company mismanagement, which is an internal reason for company failure. R3 is endorsing this position as they reported that 56 per cent of companies fail due to mismanagement.[46] Mismanagement led more than half companies to failure therefore, this is an issue that should not be overlooked. This predicament is possibly engendered by the fact that a large majority of directors in the UK are not trained or qualified for the job.[47] The future prospects of an enterprise can be compromised when it is controlled by the same management as prior to insolvency.[48] A myriad of debates have occurred on whether it would be more conducive to keep the directors in place or completely remove them while there is an attempt to bring the company back into recovery.[49]

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[41] On wrongful trading see *Re Purpoint Ltd* [1991] BCC 121.
[42] Trevor Byrne, 'Credit Management and Cash Flow in Business' Recovery (Spring 2007) 38.
[43] *Re A Company (No.006794 of 1983)* [1986] BCLC 261.
[44] Kristin Van Zwieten, *Goode on Principles of Corporate Insolvency Law* (5th edn, Sweet & Maxwell 2019) 155.
[45] [2013] UKSC 28.
[46] R3, 'Bad management to blame for nearly 60% of corporate insolvencies' <https://www.r3.org.uk/index.cfm?page=1114&element=12964> accessed 08 February 2019.
[47] Finch and Milman (n 8) 126.
[48] Graham Review into Pre-pack Administration, Report to the Rt Hon Vince Cable MP, June 2014. <https://www.gov.uk/government/publications/graham-review-into-pre-pack-administration> accessed 22 May 2019; A further discussion about the application of the recommendations see Chapter 4, Section 4.5.2.
[49] About the impact of rescue to directors see Chapter 2, Section 2.4.2.2; for a debtor-in-possession approach see Chapter 6, Section 6.2.1.

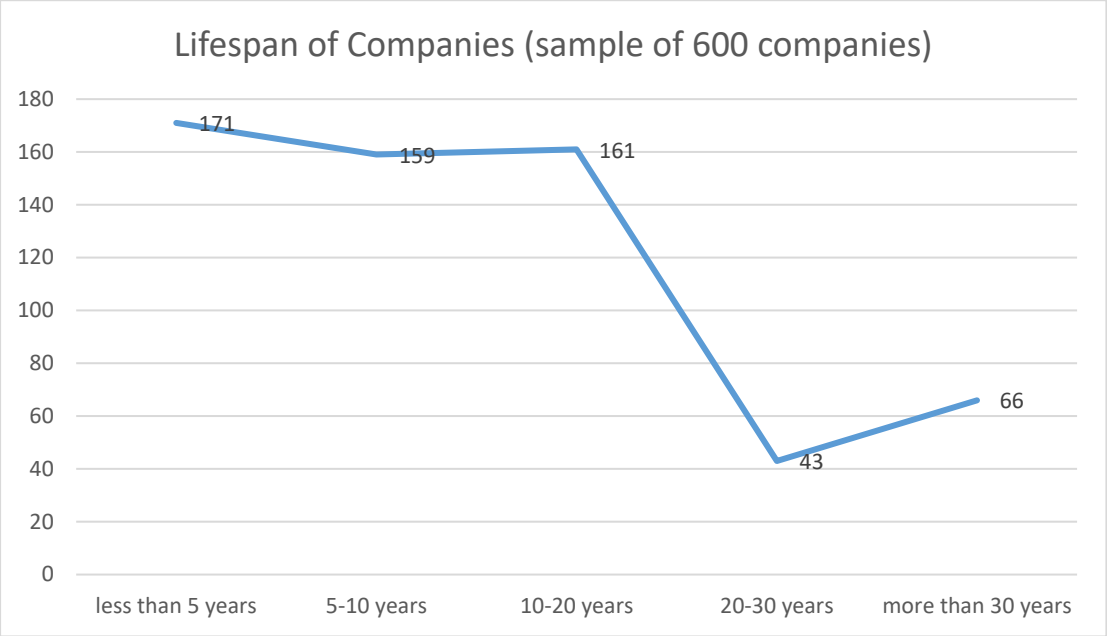
Americans are under the impression that mainly external factors cause corporate distress and that a rescue procedure is deemed to be effective when company rescue is attained.[50] The factors that could trigger the collapse of the company are understood differently in the UK, since it is widely acceptable that endogenous factors can influence the solvency state of a company.[51] UK insolvency experts usually believe that business rescue is a better result than rescuing the company.[52] Evidently, insolvency can be averted only with radical changes within the company, which could include, *inter alia*, a new company management and changes in the economic activities of the company.[53]

2.3.1 Do most companies come to an end while they are young?

In the 1970s, Argenti created a model that was formed by the types of companies that are susceptible to failure.[54] The corporation categories are the high rollers, larger companies and small companies. The high rollers are the companies with a pioneer business plan where their turnover is augmented rapidly. In due course the aftermath for these companies is that they overtrade and then they ultimately become insolvent.[55] The large companies category are commonly mature public companies that are managed by professionals, which became lethargic and are not interwoven with the requirements of the market anymore thus, they are led to failure. The problem with small companies is that they never go beyond the poor level of performance. Albeit in small companies

[50] Jay Westbrook, 'A comparison of bankruptcy reorganization in the US with the administrative procedure in the UK' (1990) I.L & P. 86, 88; Van Zwieten (n 44) 480; Chapter 6 deals with this issue.
[51] Cork (n 24) 202-203.
[52] Ron Robinson, 'Proposals, proceedings and preferential status' Recovery (March 2002) 38.
[53] Belcher (n 4) 24.
[54] John Argenti, *Corporate Collapse: The Causes and Symptoms* (McGraw-Hill 1976) Chapter 8.
[55] Clare Campbell, Brian Underdown, *Corporate Insolvency in Practice: An Analytical Approach* (Paul Chapman Publishing 1991) 23-25.

the owner is usually determined and knowledgeable s/he does not have the experience to deal with business and financial matters during a period of distress.[56] Consequently, small companies usually collapse while they are young and this is a significant matter that is empirically evaluated and discussed below.[57]



Graph A[58]

Companies that have been registered in the last few years are arguably more prone to insolvency.[59] An evaluation of whether companies fail while they are young is done through a comparison of graph A companies with their rescue outcomes. According to graph A, 330 out of 600 companies went into administration in their first 10 years therefore, the premature years of the company are critical. Only one out of those 330 companies attained rehabilitation and avoided liquidation or dissolution. If company rescue is viewed as the ideal rescue outcome, these companies have experienced a total

[56] Ibid.
[57] John Hudson, 'The Age, Regional, and Industrial Structure of Company Liquidations' (1987) 14 Journal of Business Finance & Accounting 199-213, 199.
[58] From the quantitative database that was formed by the author of this thesis.
[59] Robert Cressy, 'Why do Most Firms Die Young?' (2006) Small Business Economics Vol. 26, No. 2, 103-116; Finch and Milman (n 8) 123-124, 141.

failure. These numbers might be misleading since this analysis is not necessarily suggesting that all these companies have failed. Approximately the 30 per cent of companies that were 10 years old or below sold their business. The sale of assets as piecemeal reaches the 70 per cent, which shows that a substantial number of companies fail.

The above percentages can be compared to the study of Wilson, Wright and Altalnar about the lifespan of companies before liquidation.[60] They revealed that 30 per cent of companies that were registered in 1999 were liquidated in less than three years, while 67 per cent of these companies entered liquidation in less than 10 years. Newly established companies are more susceptible to insolvency because the interest rates are higher for them. Due to the limited life endurance of these companies, they did not have the opportunity to collect their profits and have fixed contracts with their customers and suppliers.[61] Hudson highlights that the state of the company is usually jeopardised from year two until year nine as several companies from his study entered liquidation within those years.[62] This tactic precludes the incapacitated companies that lack economic development.[63]

2.3.2 Creative destruction?

The disintegration of companies is unavoidable, and several commentators are also supporting that this is *de rigueur* for the economic market to be procreative. The presence of zombie companies can weaken the circumstances. The existence of vastly

[60] Nick Wilson, Mike Wright, Ali Altalnar, 'The Survival of Newly Incorporated Companies and the Impact of Founding Director Characteristics' (2014) 32 International Small Business Journal 733-758.
[61] John Hudson, 'Characteristics of Liquidated Companies' (1982) Mimeo, University of Bath.
[62] Ibid.
[63] Brown (n 11).

deteriorated companies within the market could vitiate healthy companies and eventually lead them to insolvency.[64] In the modern economy any company could fail but there is usually a reason behind the collapse. This should not be automatically viewed as ominous though. The following example reinforces the view that the collapse of a company is not a completely negative situation.

A restaurant that is on the verge of insolvency, needs to evaluate the available options to be kept afloat.[65] The restaurant is located in a side road in a small town in England with an owner whose skills to operate a restaurant business do not reach the optimum level. The price of the food is really high and does not go hand in hand with the food quality. There is constant turnover of the employees and particularly of waiters who are receiving low gratuity due to the dissatisfaction of the customers. Since the employees might not have enough incentives, bad customer service is the outcome. If this company continues trading under these arduous circumstances, the owner will be unable to repay the creditors. This is creating a domino effect for the business and thus, liquidation would be in the best interests of creditors. Most stakeholders are not profiting from the company and this would mean that the possible closure of the restaurant cannot worsen their position. Another example is set below by interviewee 2[66] who expressed the following:

> "Pick a fashion retailer that chooses to close some of its stores. Is it just the stores that is making it unviable or is it that its product is rubbish, that its product is out of fashion, low stock, delays in the changing of the fashion just not in

[64] Nick Hood, 'The inexorable rise of Britain's army of the walking corporate dead' (2013) 6 C.R. & I. 180-181.
[65] Douglas Baird, 'A world without bankruptcy' (1987) 50 Law and Contemporary Problems 172-193, 182.
[66] Interviewee 2 (Insolvency Practitioner), Big Four (Leeds, UK, 14 December 2018); see Appendix D.

> trend, in the wrong location and maybe that comes back to location and leases. Is it because its pricing structure is totally wrong? It is neither cheap or high end, stuck in a middle and no one really wants it. You probably have to do other things in the business such as cutting costs, changing your pricing structure and making sure that what you are selling is desirable and viable."

The interviewee gave a paradigm about a fashion store which has contiguous issues with the restaurant example. The problem in most situations can be found at the core of the business. Therefore, the owners need to have a restructuring plan that would promote a viable future for the subject matter type of business. The restauranteur could take another approach by changing the food offerings and finding cheaper suppliers to reduce costs. Yet, the reputation of the restaurant has already deteriorated and the value of the business as well as the quality of the food could become poorer. Rescue is not always ideal according to the above examples, since most stakeholders would be better-off if the company was liquidated. Specifically, the chef and the waiters would receive more appreciation from another restaurant, the creditors would receive some of the owed debt since the restaurant equipment will be sold and the owner could be well-off in another type of business. Company liquidation could be described as 'creative destruction' which is a term that arises from economics and was initiated by Schumpeter.[67] The monopolistic structures should be discouraged though by promoting rescue.

[67] Joseph Schumpeter, *Capitalism, Socialism and Democracy* (Harper & Brothers 1942) CHAPTER VII.

Companies should be in search of possible outcomes instead of pursuing the ideal one, since this is doubtfully feasible.[68] Herbert Spencer after reading about the Darwinian theory paralleled it with economic theory and what followed is that he coined the term 'survival of the fittest'. [69] Darwinian theory can be applicable to human societies and thence, on companies. This pinpoints that when companies do not evolve and adapt with the contemporary approaches of the market and society, their failure will be eventual.[70] Argenti embraced this in his analysis about the capitalist economy in which he supported that the weak companies must perish to pave the way for stronger companies to grow.[71] Gross in the 1990s kept the same view who pertained to it as 'bankruptcy Darwinism'.[72] She believed that only companies that are compatible with the interests of the community and are capable of overcoming financial distress should be sustained.[73] Hyman agrees through divulging that: "In this market, growth can only come from capturing market share from rivals. Those retailers with strong customer propositions and management teams able to adjust to this new competitive landscape will do very well."[74]

New technology has been an integral part of Schumpeter's theory, which makes creative destruction more eminent.[75] An obvious paradigm of this development is the evolution of the internet during the past decade. This technological development

[68] Sandra Frisby, 'Insolvency Law and Insolvency Practice: Principles and Pragmatism Diverge?' (2011) 64 Current Legal Problems 349-397, 366, 368.
[69] John Gray, 'A Point Of View: Why capitalism hasn't triumphed' BBC (8 November 2014) <https://www.bbc.co.uk/news/magazine-29951222> accessed 24 March 2019.
[70] Tim Verdoes, Anthon Verweij, 'The (Implicit) Dogmas of Business Rescue Culture' (2018) 27 Int. Insolv. Rev. 398–421, 399; Christopher Frost, 'Bankruptcy Redistributive Policies and the Limits of the Judicial Process' (1995) 74 N.C. L. Rev. 75-139.
[71] Argenti (n 54) 170.
[72] Karen Gross, 'Taking Community Interests into Account in Bankruptcy: An Essay' (1994) 72 Washington University Law Quarterly 1031, 1035.
[73] Ibid.
[74] Richard Hyman, 'The changing face of retail' Recovery (Spring 2012) 17.
[75] Thomas McCraw, *Prophet of Innovation Joseph Schumpeter and Creative Destruction* (Harvard University Press 2009) 54, 254.

resulted in hitting high street and mall retailers as well as restaurants as online shopping became more prominent.[76] This had consequential impact on rents that practically caused continuous problems to landlords.[77] Technological development also led in substituting businesses like video rental companies with online streaming services and platforms. The value of technology innovation to business was also accentuated by COVID-19 as there is a continued growth of online businesses that is creating further pressure on brick business infrastructures. Venture capitalists often say business innovation is fuelled by technology innovation; the combination of both supports sustainable existence of companies. It is natural for companies that to do not evolve the advancement of technological tools to be replaced from that are hand-in-hand with companies that follow that technology.

This approach suggests that rescue should be selective and that not all companies are worth saving. The Cork Committee supported that businesses should be rehabilitated only in occasions where it is propitious to the economic development of the nation.[78] The 1999 DTI Review aligns with this opinion as it noted that rescue should only take place when there are viability prospects.[79] The intention of the legislator was not to maintain companies that could have a negative impact over the economic market of the country. In other words, company failure is a necessary evil for the market to work effectively. Although other jurisdictions view rescue as a right that all companies should have,[80] the method that the UK follows is that not all companies should have the right of being saved.[81] Dying companies could limit the chances for

[76] On a certain extent this was predicted by Schumpeter. For this see Joseph Schumpeter, *Can Capitalism Survive: Creative destruction and the Future of the Globe* (Harper Collins (Harper Perennial Modern Thought 2009) 46.
[77] See Chapter 3, Section 3.7 for the problems of landlords in the context of CVAs.
[78] Cork Report (n 5) para 198 (j).
[79] A Review of Company Rescue (1999) (n 23).
[80] Such as Chapter 11 in the US.
[81] Frisby, 'In Search of a Rescue Regime' (n 2) 248.

other companies to thrive.[82] With the existence of limited resources, major challenges would have occurred if the right of rescue was offered. Thus, some companies – such as zombie companies[83] – should directly be liquidated instead of pursuing a solution that would just delay the eventual collapse of the company.

Economic failure is often linked to legal failure, which forces the company to take action instantly whether this is liquidation or a corporate rescue procedure.[84] Even though the efforts of saving a company could be unavailing and should only be sought selectively, this does not mean that rescue should not be encouraged.[85] Belcher asserts that rescue is "a major intervention necessary to avert eventual failure of the company"[86] yet the real meaning of intervention is ambiguous. Various factors could cause a company catastrophe therefore, this chapter illustrates the company rescue options.

2.4 Business rescue or Company rescue?

The aim here is to comprehend the functioning of rescue and the consequences that might ensue in the process. The problems that might arise in the pursuit of fulfilling this will be evaluated along with an estimation on whether company rescue can deliver a total rescue of the company as a whole. Various scholars and professionals argue that a successful rescue does not necessarily mean that the company should come out of the procedure intact.[87] It is also maintained that company rescue is only successful when

[82] James White, 'Death and Resurrection of Secured Credit' (2004) 12 American Bankruptcy Institute Law Review 139, 151; McCormack (n 35) 111.
[83] For an analysis about the zombie phenomenon see R3, 'The 'zombie businesses' phenomenon: An update' (January 2014) <https://www.r3.org.uk/media/documents/policy/research_reports/special_reports/R3_Zombie_Report_Jan_2014.pdf> accessed 17 February 2020.
[84] Campbell and Underdown (n 55) 17.
[85] McCormack (n 35) 131.
[86] Belcher (n 4) 12.
[87] Ron Harmer, 'Comparison of Trends In National Law: The Pacific Rim' (1997) 23 Brook.J.Int'lL.146.

there is a long-term company survival.[88] Maybe a better description for a company rescue would be that there is a corporate repair and for a business rescue is that there is corporate recycling.[89] A distinction between company rescue and business rescue is drawn as their application and outcome is substantially different.

2.4.1 Can the survival of the business produce a more beneficial collective outcome?

A company rescue procedure cannot have the same lucrative results in all jurisdictions as the background of each country is different and it is possible that the legal system will not be capable of supporting that mechanism. There is always the mutual component of formal procedures though, which is to provide a new lease of life to the enterprise. It is arguably more ideal to save the company, as with the company, the business or part of it will also survive.

Company rescue has been characterised as 'pure rescue' and if strictly speaking, it means that the company should be rehabilitated and at the same time it should come out of a process without having any sort of damage.[90] This signifies that pure rescue should comprise a healthy entity that will carry out the exact same activities, the employees will be kept and the owners should remain the same.[91] This is not an actual delineation of company rescue as some of the employees could be made redundant and the main activities of the company could be subject to alteration.[92] Company rescue could involve streamlining operations, renegotiating liabilities and procuring new finance. Even if company rescue is attained Campbell suggests that "the 'survivor' may

[88] Belcher (n 4) 23.
[89] Frisby, 'Insolvency Law and Insolvency Practice' (n 68) 363.
[90] Frisby, 'In Search of a Rescue Regime' (n 2) 248.
[91] Ibid; Belcher (n 4) 22-23.
[92] Ibid.

have the same name as before but may be different in many other ways."[93] The office-holder in an attempt to bring the company back into profitability either changed the structuring of the company or came into an agreement with the creditor by waiving-off some part of the debt and/or continuing to repay them with monthly instalments. Even if the company is saved and continues trading with the same name, it will most likely never be the exact same company as it was before the financial difficulties.[94]

When a company is in trouble, the director must act instantaneously as this means that the resources of the company have been diminished hence, those resources must be utilised wisely. The focus must be on the profitable part of the business that must be separated from the ailing business swiftly and efficiently.[95] The company is just the shell of the business that is responsible for trading, employment or produces revenues.[96] In other words, the company is the cover of the business whereas the business is comprised by *inter alia* the employees, the receivables, the assets, the stock in trade, the work in progress, the executory contracts and the suppliers. An attempt to rehabilitate the company, besides the fact that it requires early decision making, can provoke restrictions in terms of using the assets in a more procreative way[97] and the outcome for creditors might not be as efficient as in a business sale.[98] Even company rescues can be described as partial rescues,[99] therefore, the fact that business rescue is in all occasions partial should not be viewed negatively.

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[93] Andrew Campbell, 'Company rescue: the legal response to the potential rescue of insolvent companies' (1994) 5 I.C.C.L.R. 16-24.
[94] Sandra Frisby, 'A preliminary analysis of pre-packaged administrations' (R3: Association of Business Recovery Professionals, 2007).
[95] Stuart Slatter, David Lovett, *Corporate Turnaround: Managing Companies in Distress* (2nd edn, Penguin Group 1999) 221.
[96] Rizwaan Mokal, 'Administrative Receivership and Administration—An Analysis' (2004) 57 Current Legal Problems 355-392, 360; Vanessa Finch, 'Re-invigorating corporate rescue' [2003] J.B.L. 527-557, 531.
[97] For example, restrictions might be imposed by lenders through financing agreements.
[98] Robinson, 'Proposals, proceedings and preferential status' (n 52).
[99] Belcher (n 4) 23.

Rescue can be achieved through different means and the outcome could be that the company continues with the same operations or that the company is restructured, or new financing is injected, or it is downsized or parts of the business are sold-off, or there is a company takeover.[100] The business of the company can be saved by dividing the viable part of the business from its liabilities and sell it as a going concern to a Newco.[101] This does not necessarily mean that it will be sold to new owners. The success of a rescue procedure is linked with the long-term survival of the company and better returns for creditors.[102] The long-term endurance of the company cannot be guaranteed though. Even if all the right policies, right laws and right management for Newco are in place, it is possible that a macroeconomic event can still destroy the Newco. The period right after a company is saved through a rescue procedure is critical. Several of these companies might have to use a rescue procedure again as the financial problems might resurface. Belcher argues that: "A successful rescue should bring about not only survival in the short-term but also sustained economic activity in the long-term."[103] 24 out of 600 companies that used administration also entered a CVA or an administration in the past.[104] If contemplated that in the sample of 600 companies only 3 companies had a corporate rescue, 24 out of 600 is a lot. Although the volume of companies that had a pre-CVA or a pre-administration is limited, there are some interesting conclusions that were deducted from the analysis of these variables. None of them managed to save the company or part of it, while half of them ended up in an asset realisation. It seems, however, that the other half of companies managed to sell the business or part of it.

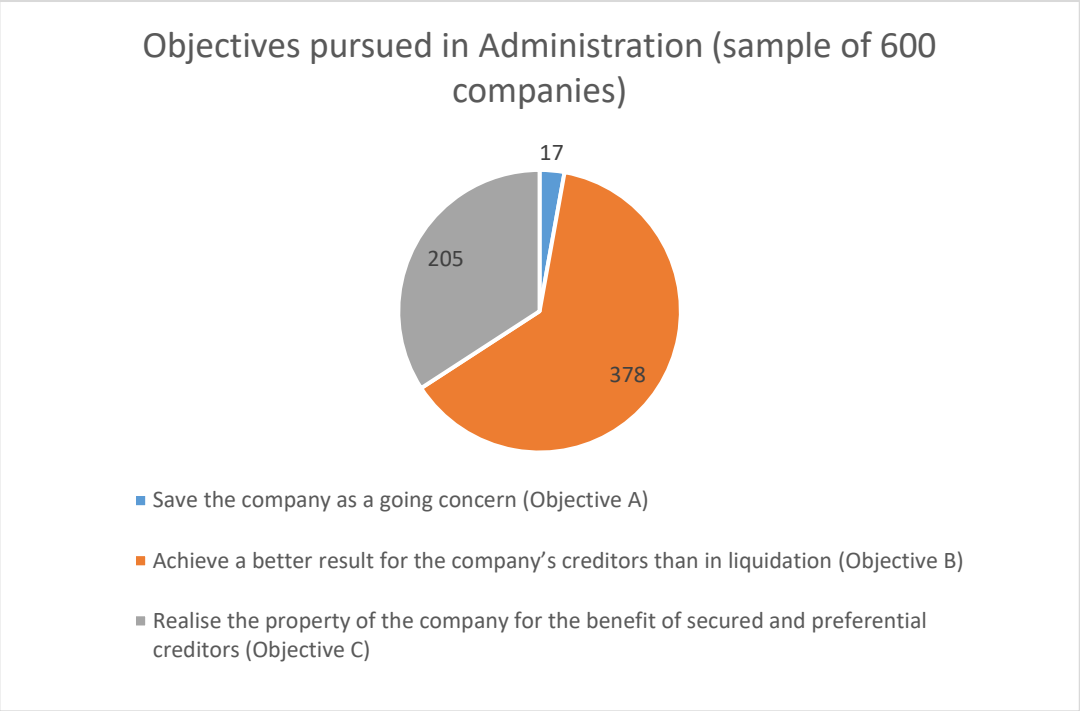
[100] Ibid 24-34.
[101] Frisby, 'In Search of a Rescue Regime' (n 2).
[102] Ibid; A Review of Company Rescue (1999) (n 23).
[103] Belcher (n 4) 23.
[104] In accordance with the database of the author of this thesis.

A new party can undertake the business after it is saved. Eventually, the long-term survival of the company is more feasible when the profitable part of the business is handled by an unconnected party.[105] Sales to connected parties could generate unwanted repercussions for the company, which is a matter that was scrutinised in the Graham Report.[106] It is not a real rescue if the company is not put into a semi-permanent solvent state. Zimmerman stated that: "the endurance of the recovery should also be considered in determining whether success or failure has been achieved. A turnaround of a year or so is not much of a turnaround."[107] When company rescue is attempted it is usually kept by the same owners and the auditor will have to reorganise the balance sheet of the company, which is considered as an onerous task.[108] Loss of employment can also take place in a business sale, as it happens when the company is rescued.

UK law on administration suggests that a going concern rescue of the company is the primary objective.[109] It even goes further to say that if company rescue is not practicable, then business rescue should be the next goal.[110] A reason that the legislator chose company rescue to precede business rescue was to trigger the director's incentive to undertake administration.[111] According to Djanogly: "Assuming that the directors are shareholders, they would normally have every reason to want to save the company rather than the business, because then they would not lose their investment."[112] The lack of this objective and generally of administration could cause grave consequences to the system as this could result in encouraging the directors to continue trading in financial

[105] Walton and Umfreville (n 3).
[106] Graham Review into Pre-pack Administration (n 47); see Chapter 4, Section 4.5.2.
[107] Frederick Zimmerman, *The Turnaround Experience Real-world Lessons in Revitalizing Corporations* (McGraw-Hill 1991) 22.
[108] DTI 2000 (n 30) 50.
[109] IA 1986, Sch B1, para 3(1)(a) (Objective A).
[110] IA 1986, Sch B1, para 3(1)(b) (Objective B).
[111] Mark Phillips, Jeremy Goldring, 'Rescue and reconstruction' (2002) 15 Insolv. Int. 75-78; John Armour, Audrey Hsu, Adrian Walters, 'The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings' (December 2006) Insolvency Service Report, 22.
[112] HC Standing Committee B, 9 May 2002, col. 549.

difficulties. Consequently, there would be further delays in attempting to rescue the corporation and as a result this could transmute into an impossible task.[113]



Graph B[114]

Objective A clearly states that the purpose is to rescue the company as a going concern, which means that it facilitates company rescue in which the whole business or part of it can be saved.[115] Although the option of saving the company as a going concern is there as the first hierarchical objective, graph B above shows that only 17 companies out of 600 companies that went into administration chose this path. This means that approximately 3 per cent of companies are confident enough to even attempt to rescue the company. The mere survival of the company shell without the business, should not be designated as a satisfaction of the objective.[116] The accomplishment of objective A,

[113] Carruthers and Halliday (n 1) 286.
[114] In accordance with the database of the author of this thesis.
[115] See Chapter 4, Section 4.2.1.
[116] Phillips and Goldring (n 106) 76; Hansard, House of Lords (29 July 2002), Series 5 Vol. 638, cc765-766.

can transform to be even harder.[117] Graph C below confirms this through illustrating that only 3 out of the 600 companies managed to save the company or part of the company. This objective acts not only as an impetus for directors to take action but in some circumstances, there are companies that need to keep their name intact.[118] Thus, this option should remain available. Furthermore, confidence is put on business rescue[119] since it is easier to be accomplished owing to the hiving down, in which the liabilities of the business can be separated from the productive part of the business.[120]

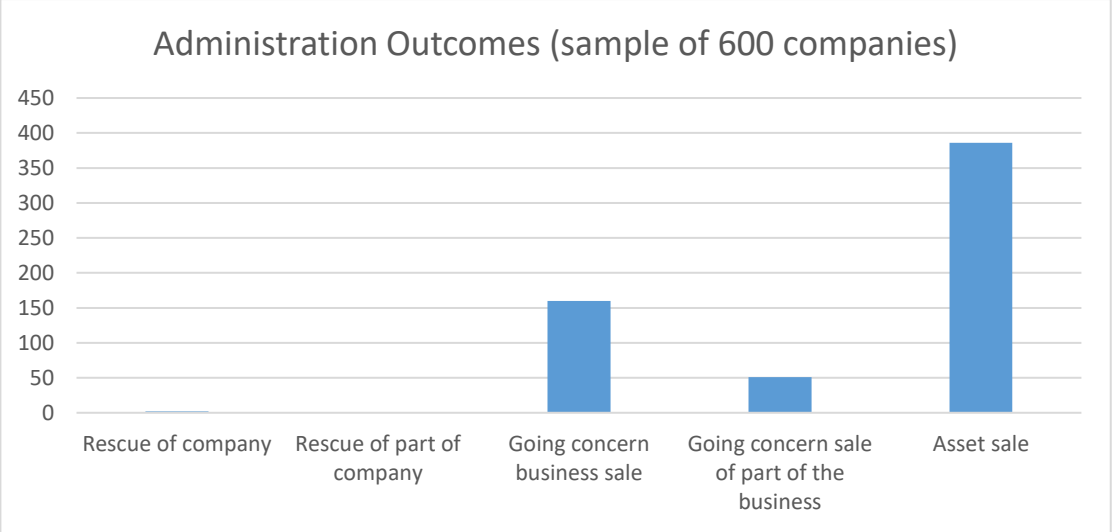
While discussing with interviewee 8[121] that only 17 companies were capable enough to have objective A as their priority and only 3 of those companies managed to keep the company sound, he mentioned that:

> "I think administrations which have been in the UK legislation for 30 years are very successful at saving businesses and they are relatively easy to get into as a process, they are not too dominated by the court, they provide flexibility, the general business community and the public understand what is meant by administration generally speaking and they have far better connotations of other types of insolvency such as liquidation so I think they have been successful. They have not been successful in terms or rescuing the company so the difference between the company and the business rescue is important. It is very difficult in most jurisdictions to rescue a business and a company at the

[117] Alan Katz, Michael Mumford, 'Study of administration cases' (2007) 20 Insolv. Int. 97-103.
[118] Businesses that usually need to retain the entity are structured groups companies or football clubs.
[119] Ron Robinson, 'The Enterprise Bill moves on' Recovery (Autumn 2002) 42.
[120] Van Zwieten (n 44) 480.
[121] Interviewee 8 (Insolvency Practitioner) Big Four (London, UK, 19 January 2019); see Appendix D.

> same time because it is hard to deal with all the legacy issues which have meant that the company has gone into insolvency in the first place. Having said that, the original legislation was designed to rescue the company as well as being a primary objective and if I have done 100 administrations over the last 20 years, I have achieved that purpose probably only once."

The statement of the interviewee about dealing with a low number of companies that managed to be rescued during the past two decades seem to fit with the outcome of graph C. This graph illustrates that only 0.5 per cent of those companies were rescued. This is suggesting that administration is not designed for strictly saving companies.



Graph C[122]

As seen in graph C, administrations usually result in the realisation of the company assets for the benefit of secured and preferential creditors. AR was abolished but it can still be distinguished through objective C and its outcomes.[123] Although the purpose of the Cork Committee was to promote rescue culture through facilitating company survival, it is strenuous to pass that threshold. Graph C also shows that approximately one out of three companies saved their business or part of their business in administration. Albeit, the Cork Committee prioritised company rescue, they also conveyed that if a company is insolvent, it would be socially salutary and justifiable to rehabilitate the enterprise instead of the company.[124]

Company salvation as a going concern is rarely the case, while business rescue is an easier and more attainable task. Frisby's results on the outcome of administration have shown that only 1 per cent of 366 companies post-Enterprise Act 2002 had

[122] In accordance with the database of the author of this thesis.
[123] Kayode Akintola, David Milman, 'The rise, fall and potential for a rebirth of receivership in UK corporate law' (2019) Journal of Corporate Law Studies <https://www.tandfonline.com/doi/full/10.1080/14735970.2019.1631551> accessed 29 September 2019; See Chapter 4, Section 4.2.3.
[124] Cork Report (n 5) para 193.

company rescue as an outcome.[125] This empirical research that was conducted over 10 years ago does not diverge a lot from the quantitative analysis of this thesis as the results adduce to be undeviating. When interviewee 2[126] saw the results of graph C he had the following interesting conclusions:

> "… rescuing the company or part of it is a bit peculiar. If you can sell the shares anyway, the company would not necessarily have to go into administration because the cost of buying the business is taking all the debt burden, all the liability, the very thing that has caused the administration so, that is why there are very few ... So that is a really peculiar situation and the reason you only got a handful is for that. Rescuing the business and assets whether in whole or part is just a function of is there a buyer out for that business? Do you get to the right people at the right time?"

What this interviewee is articulating is that the empirical results are sensible since according to his professional experience in practice, company rescue happens only in extraordinary junctures. While graph C is suggesting that the realisation of assets reaches 386 companies, business rescues or part of them are estimated at 211 companies. Most companies end up in an asset sale, but a considerable percentage of the business of companies is sold. Approximately 35 per cent of companies that use administration end up in a business sale. Hence, if business rescue is seen favourably,

[125] Sandra Frisby, 'Interim Report to the Insolvency Service on Returns to Creditors from Pre- and Post-Enterprise Act Insolvency Procedures' (July 2007).
[126] Interviewee 2 (n 65).

this percentage is denoting some level of success. Interviewee 7[127] further maintains the results of graph C through stating the following:

> "If you think about outcomes, it is almost never the case that a company that goes to an insolvency procedure will come out the other end as a solvent company. The business will survive but not the company and as you know in the UK that has always been the approach unlike the USA approach where it is trying to save the company. What we are trying to do is to save the business and I personally see it as a more useful, simpler and easier process to operate than trying to save the company which is insolvent because if you are going to try and save an insolvent company you essentially have to restructure its balance sheet …What is the best way to save the business? The best way to save the business is to transfer it from those who fail to those who will essentially do a better job with it."

The approach in each country is varying since the nature of the perception and incentives can be substantially different.[128] Should a company rescue procedure be viewed and considered as a method for ensuring that the aftermath for stakeholders will be better, or should it have an aim to save the company first? For this question to be answered the mindset and incentives of the main stakeholders should be discovered.

[127] Interviewee 7 (Lawyer/Academic) a law firm and a UK university (London, UK, 15 January 2019); see Appendix D.
[128] See Chapter 6, section 6.2.2.2 for a further discussion.

2.4.2 The perspective of stakeholders towards rescue

Even though a company is an artificial person, it is the close parties that can influence the fate of the distressed company. The main actors that can be directly involved are not only the secured creditors but also stakeholders such as the workforce, directors, suppliers and other unsecured creditors like the Crown.[129] The affected parties of the distressed parties can interpret corporate rescue differently. The shareholders and employees of troubled companies view company rescue in a more salutary way than creditors or managers. Full restoration is unusual but at the same time possible. The most sensible outcome though is that the main parties of insolvency will not be fully reinstated even if the rescue succeeds.[130] Finch supports that the three elements that need to be satisfied for a rescue regime to operate accurately, are to provide the relevant information that would enable the appropriate utilisation of supplies; generate strategies; control that would assist rescue; and to take action at the proper timing.[131] The success of rescue extensively depends on the key actors of the company.

2.4.2.1 Banks

The viewpoint of secured creditors – who are usually banks – play a crucial role as regards the acceptance and successfulness of a procedure. The decisions of banks as well as their cooperation can affect rescue since their standpoint is strong during a company's insolvency state.[132] The British Bankers' Association demonstrated that a rescue attempt without the collaboration of creditors leads company survival to a

[129] For December 2018 announcement to restore Crown preference for certain debts see HM Treasury, Budget 2018 (HMSO, 2018), HC Paper No.1629; Harmer (n 84) 146.
[130] Ibid Harmer 144.
[131] Vanessa Finch, 'Control and co-ordination in corporate rescue' (2005) 25 Legal Studies 374-403, 376.
[132] Belcher (n 4) 155.

deadlock.[133] Although the debt recovery of banks depends on the decisions of IPs, concurrently the banks are closely observing the procedure.[134]

Banks have a critical role in the establishment of a rescue procedure as their outlook would be pivotal regarding the prospects of any insolvency procedure.[135] In other words, the success of any procedure is extensively depending on the intention of banks regarding their utilisation thus, it is significant to generate bank incentives.[136] Finch manifests that for a new mechanism to be effective it will "require a change of mindset or fundamental ideas" of banks.[137] The introduction of the streamlined administration has as a purpose an orientation towards a collective approach and to give a higher priority to rescue.[138] Back in 2003 there were doubts that floating charge holders would embrace the new administration,[139] but there was also the contention that the winner of this change would be the banks.[140] Even though post-EA 2002 floating charge holders were cautious about using administration – mostly because they believed that AR was a better tool for them – it now seems that they are content with the mechanism.[141] When IPs need to choose between company and business rescue, they will choose the one that satisfies the collective interests of the creditors.[142] In most cases the salvation of the business provides the best available outcome for creditors as a whole.[143] Arguably, the new administration is a hybrid of the pre-EA 2002

[133] British Bankers Association (n 8).
[134] Rebecca Parry, 'United Kingdom: Administrative Receiverships and Administrations' in Katarzyna Gromek Broc, Rebecca Parry (ed.), *Corporate rescue: An overview of recent developments from selected countries* (Kluwer Law International 2006) 174.
[135] John Alexander, 'The Enterprise Act 2002' (2003) 19 I.L. & P 3.
[136] Vanessa Finch, 'Corporate rescue: who is interested?' [2012] J.B.L. 190-212.
[137] Finch, 'Re-invigorating corporate rescue' (n 93) 538.
[138] DTI/Insolvency Service White Paper, *Productivity and Enterprise 'Insolvency – A Second Chance* (Cm 5234, 2001).
[139] Stephen Davies (ed.), *Insolvency and the Enterprise Act 2002* (Jordans 2003) 71.
[140] John Willcock, 'How the Banks Won the Battle for the Enterprise Bill' Recovery (June 2002) 24-26.
[141] See Chapter 4, Section 4.2.3 and 4.9.
[142] Van Zwieten (n 44) 479.
[143] Explanatory Notes to the EA 2002, para 647.

administration and AR since creditors can exploit administration in the same way as AR but with some extra features.[144]

When banks are given enough control, their perception towards the rescue procedure would be approving. Usually, an extensive power of controlling struggling companies is provided to floating charge holders. They have now the ability of appointing an administrator of their choice and if the administrator is appointed by another party, the floating charge holders have the capability of choosing an IP that they consider more appropriate.[145] It seems that in most administrations the banks have a "close relationship" with the chosen IP.[146]

Secured creditors have an important role towards rescue as they could be the main source of funding that would allow the company to utilise administration. A vast amount of funding comes from fixed charge holders, but funding through factoring could also allow access to the insolvency process.[147] Obtaining funding that would make trading available is crucial since trading maximises the company value. An example of motivating companies to provide such funding is super-priority. Several recommendations regarding this matter have been made about super-priority but no legislative provisions have passed.[148]

The position of the banks when the company is near insolvency is onerous thus, they ensure that continuous updates are received about the level of deterioration of the

[144] Willcock (n 137); see Chapter 4, Section 4.2.3.
[145] EA 2002, Sch 16, paras 14, 18(3), 36(2); also see Kayode Akintola, 'What is left of the floating charge? An empirical outlook' (2015) 7 JIBFL 404.
[146] Office of Fair Trading, *The Market for Corporate Insolvency Practitioners* (OFT 2010).
[147] Vanessa Finch, 'Doctoring in the shadows of insolvency' (2005) J.B.L. 690-708, 697.
[148] The Insolvency Service, Encouraging Company Rescue – a consultation, (June 2009); The Insolvency Service, A Review of the Corporate Insolvency Framework response form (25 May 2016); Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) 5.156-5.168; for further see Chapter 4, Section 4.7.

company.[149] Through this knowledge they take actions that would benefit their own interests. Creditors do not have an interest on preserving the company since they are focusing on receiving better returns.[150] Yet, there could be a win-win situation when the outcome for creditors is better through rescuing the company and/or business rather than liquidation. This can also operate as an incentive for secured creditors, but they will need to be patient as the returns are usually not instant.[151]

2.4.2.2. Directors

The company management usually takes the blame for the company crisis either because the wrong decisions were taken or because their timing was incorrect. Since directors have a duty towards creditors they are responsible for pursuing a solution that would aid the company to overcome financial crisis. Wrongful trading is regulating this and its punitive concept is possibly signifying that there is an orientation towards rescue instead of creditors.[152]

Directors are hesitant to take early intervention and that leads to limited chances of rescue.[153] R3 recorded that 77 per cent of companies were already in an irreversible condition when the professionals took over.[154] Creditors and IPs in the UK usually argue that the director is not the most suitable person to handle a rescue procedure since they already had their chance of informally turning around the company.[155] Finch concluded that: "Corporate managers may also embark on a project so large that its failure will

[149] Finch, 'Corporate rescue: Who is interested?' (n 133) 195.
[150] A Review of Company Rescue (1999) (n 23); Frisby, 'Insolvency Law and Insolvency Practice' (n 68) 360.
[151] Finch, 'Re-invigorating corporate rescue' (n 93) 531.
[152] Adrian Walters, 'Enforcing Wrongful Trading: Substantive Problems and Practical Disincentives' in B Rider (ed.), *The Corporate Dimension* (Jordans 1998) 145-160, 149; Finch and Milman (n 8) 602.
[153] Parry (n 131) 175.
[154] R3, Ninth Survey of Business Recovery (2001); Finch and Milman (n 8) 204.
[155] Finch, 'Corporate rescue: Who is interested?' (n 133) 203.

place the survival of the company at risk."[156] Interviewee 7[157] supported that directors should not take part in the rescue procedure through stating the following:

> "If a company is unable to pay its debts, in my mind the board of directors has failed. In my opinion, it should be a licenced insolvency practitioner who needs to take over the business in order to deal with it properly because he is someone who has the knowledge and understands what needs to be done rather than the board of directors of the company. So my view is and when you are considering outcomes, if you have a debtor-in-possession you are going to try and find a way to rescue the company and the corporate entity. That is a long and complicated job involving courts and lawyers … The business problem needs to be sorted out by business people and to my mind the best way of dealing with the issue is to recognise an insolvency practitioner who should go on and sell the business to someone who is able to carry it on better … I think that the system that is appointing insolvency practitioners and getting them to sell the assets and the business to someone else is a far better procedure than the one that is involving courts, judges and all the rest of it."

The interviewee indicated that the involvement of a trained professional during a formal rescue procedure is critical for the survival of the company and/or its business.[158] He also expressed that each country is accustomed to a different process with respect to

[156] Vanessa Finch, *Corporate insolvency law: perspectives and principles* (2nd edn, CUP 2009) 160.
[157] Interviewee 7 (n 124).
[158] See Chapter 6, Section 6.2.1.

who is controlling the company in an insolvency process. In CVAs, the directors are in control, which comes into conflict with this opinion. Yet, this can be justified since CVAs are mainly used by large companies, in which directors are usually more experienced.[159] According to the professional experience of the aforementioned interviewee, when the business is sold to an unconnected party – which can be also linked to the Graham Report – this could prevail to be more effective for the company in the long-run.[160]

The directors are discouraged to cooperate with the creditors during administration because they receive extensive attention. Banks have the power of appointing the administrator of their choice or to get the company/director to appoint the IP of their choice. The directors are reluctant to collaborate, since they believe that this could harm the company instead of alleviating it from financial difficulties.[161] The involvement of the director is required though since their knowledge about the company is invaluable. The nature of the director's position, however, is suggesting that s/he cannot have a wide influence over rescue. Since during pre-packs the business sale agreement happens in advance of the initiation of administration, directors believe that this could operate to their advantage.[162] Therefore, in this sense directors could affect rescue if business rescue is obtained under these circumstances. This could only happen though if the creditors and shareholders are backing this decision.

Directors must be wary on when their duty towards creditors is triggered. As per CA 2006, s 172(3): "The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act

[159] See Chapter 3 for a further analysis on CVAs.
[160] See Chapter 4, Section 4.5.2.
[161] Finch, 'Control and co-ordination in corporate rescue' (n 128) 391.
[162] Finch, 'Corporate rescue: Who is interested?' (n 133) 202.

in the interests of creditors of the company." If directors are in breach of this duty, the most possible outcome is that they be held culpable.[163] The decision in *West Mercia Safetyware Limited v. Dodd*[164] reinforced this statutory instrument, as it was held that when the company is on the verge of insolvency, the best interests of the general body of creditors need to be considered. *Re HLC Environmental Projects Ltd*[165] interpreted this even further since it was clarified that this duty is only triggered when the company is in insolvency or in the vicinity of insolvency. In *Dickinson v. NAL Realisations (Staffordshire) Ltd*,[166] it was elucidated that the director needs to be attentive on protecting the interests of creditors in the long-term, also in occasions where the company is solvent and this is linked to the application of general avoidance provisions.[167] In *BTI 2014 LLC v. Sequana SA*,[168] the Court of Appeal's decision took another turn. It was held that the normal company purpose is to operate for the benefit of the shareholders, and that the interests of creditors have to be considered only in circumstances where the company is insolvent or be in a grave danger of becoming insolvent. If the case is that the directors acted in good faith, then they will not be held liable.[169] This issue is controversial due to the nature of testing whether the director is liable as this is considered subjective.[170] The rise of CA 2006, s 172 cases in the recent years signifies that this is an ongoing issue and the approach should be subject to change.[171]

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[163] Andrew Keay, 'Directors' duties and creditors' interests' (2014) 130 L.Q.R. 443-472.
[164] [1988] BCLC 250.
[165] [2013] EWHC 2876 (Ch).
[166] [2019] EWCA Civ 2146.
[167] IA 1986, s 423; David Milman, 'Stakeholders in modern UK company law' (2017) 397 Co. L.N. 1-4.
[168] [2019] EWCA Civ 112.
[169] *Colin Gwyer and Associates Ltd v. London Wharf (Limehouse) Ltd* [2002] EWHC 2748 (Ch); *Charterbridge Corp Ltd v Lloyds Bank Ltd* [1970] Ch. 62.
[170] Andrew Keay, 'Financially distressed companies, preferential payments and the director's duty to take account of creditors' interests' (2020) 136 L.Q.R. 52-76.
[171] *Northampton BC v. Cardoza* [2019] BCC 582; *Ball v. Hughes* [2017] EWHC 3228 (Ch); [2018] BCC 196; *Joint Liquidators of CS Properties (Sales) Ltd* [2018] CSOH 24.

2.4.2.3 Unsecured Creditors and Crown Preferential Status

Usually unsecured creditors are the most oppressed stakeholders as they almost rank last in the waterfall,[172] which means that they are likely to be more exposed to risk.[173] The administration database showed that only the unsecured creditors of 8 out of 552 companies received 100p in the £.[174] Typically, unsecured creditors are not kept informed about the financial circumstances of the company, which makes them unable to form any sort of strategic plan thus, their own state depends on the rescue outcome of the company.[175] They are also inexperienced in terms of the functioning of rescue procedures, which makes their position confoundedly insecure in comparison to secured creditors.[176]

The prescribed part,[177] which was initiated through the EA 2002, gave the opportunity to unsecured creditors to set aside the maximum fund of £600,000 that is ring-fenced from the floating charge assets. Back then the Crown preference was abolished to enhance the position of unsecured creditors. Since unsecured creditors rank last, it seems that the prescribed part is the only route that they have that would allow them to recover some of their debt. The initiation of the prescribed part ameliorated the position of the unsecured creditors, yet its effect should not be overvalued.[178]

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[172] *Re Lehman Brothers International (Europe) (In Administration)* [2017] UKSC 38.
[173] Belcher (n 4) 156.
[174] In accordance with the database of the author of this thesis
[175] Finch, 'Corporate rescue: Who is interested?' (n 133) 197.
[176] Office of Fair Trading (n 143) para.1.14.
[177] IA 1986, s 176A.
[178] David Milman, 'Priority-related issues in the context of administering an insolvent estate: status quo or a new balance?' (2014) 363 Co. L.N. 1-5.

In 2018 the Chancellor announced the reinstatement of the Crown's preferential status.[179] This could cause the discouragement of rescue since suppliers might hesitate to continue cooperating with the company, which can cease company trading.[180] There is a reservation about this through since the prohibition of termination clauses are now included in the Corporate Insolvency and Governance Act 2020.[181] With the advancement of the Crown's returns, the suppliers might be under the impression that there will not be anything left for them. Unsecured creditors have a deciding role on whether the company will carry on trading[182] hence, their incentives should be gingerly appraised. The return of the preferential status of the Crown could also have a negative impact on the rescue outcomes of CVAs.[183] When interviewee 8[184] was asked whether the proposals about the Crown status and the prescribed part will have a bearing on rescue outcomes, he replied the following:

> "…it is a backwards step and it surprised everyone…by giving them back their preferential status, they will get more money than other people, but I don't think that it will make a difference to the type of procedure. It will make a small difference to the outcome of unsecured creditors generally because they will be second to the Crown, but I don't think they will make a difference to companies."

[179] HM Treasury, Budget 2018 (HMSO, 2018), HC Paper No.1629, para.3.87; HM Revenue & Customs, 'Consultation document: Protecting your taxes in insolvency' (26 February 2019) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/781323/Protecting_your_taxes_in_insolvency.pdf> accessed 22 May 2019.
[180] Essential suppliers that are included in Insolvency (Protection of Essential Supplies) Order 2015 are excluded.
[181] See Chapter 4, Section 4.9 for this.
[182] Finch, 'Re-invigorating corporate rescue' (n 93).
[183] See further in Chapter 3, Section 3.5.
[184] Interviewee 8 (n 118).

The limited bearing that the changes would have on unsecured creditors are also maintained by the current challenges of the prescribed part. In several situations, eligible companies might not set aside a prescribed part and even if they do it currently provides nugatory returns to unsecured creditors.[185] It also seems that the HM Revenue and Customs (HMRC) is practically engrossing all the advantages that can be generated from the prescribed part.[186]

The interests of unsecured creditors were said to be considered in the budget proposals since it was stated that the prescribed part cap will be increased to £800.000.[187] The maximum allowance of the prescribed part is rarely set aside, and this can be confirmed by database of this research since only 3 out of 50 companies that set aside a prescribed part went for the maximum of £600,000. As Akintola correctly concluded "…cases where the putative benefits of this decision would be experienced would be the exception not the norm".[188] These changes might have a further impact on rescue outcomes as the abeyance of the prescribed part can be provoked and affect the returns to other creditors.[189] Interviewee 7[190] through the following statement expressed his concerns about the issue:

> "I think that whole way in which floating charge holders are penalised at the expense of everyone is absolutely wrong …. To my mind that is just theft … I don't have a problem with the Crown preference. I mean the Crown has preference in

[185] Kayode Akintola, 'The prescribed part for unsecured creditors: a pithy review' (2017) 30 Insolv. Int. 55-58, 55.
[186] Kayode Akintola, 'The proposed preferential priority of prepaying consumers: a fair pack of insolvency recommendations?' [2018] J.B.L. 1-14, 14.
[187] Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) 1.82–1.84.
[188] Kayode Akintola, 'The prescribed part for unsecured creditors: a further review' (2019) 32 Insolv. Int. 67-70, 69.
[189] Ibid.
[190] Interviewee 7 (n 124).

> one form or another in over 100 years and I don't have a problem with the idea that the Crown should have priority in insolvency, what I have a problem with is with the Crown having a priority not only against unsecured creditors but the floating chargees. That seems to me to be wrong."

This interviewee is practically trying to find a rational reason as to why this is happening at the expense of the floating charge holder. The return of Crown preference will suppress the floating charge holder rights even further, as the Crown returns would be deducted from the floating charge assets.[191] The outranking of unsecured creditors by the state has also been of concern in the past.[192] Interviewee 1[193] expressed the following about the effect that the Crown preference return would have on creditors:

> "It might have an impact on creditors if they sense that it would tighten their lines of credit because they are more exposed and they are less likely to be paid in the event of an insolvency. So that may tighten credit, which may cause more failures rather than less."

Tribe subsequently argued that the HMRC might have not been in any consequential deliberations about the subject matter with the Insolvency Service.[194] Since these changes will not come into force before April 2020, these are merely conjectures, as a potential bearing on insolvency/rescue outcomes will only become apparent in the long-term.

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[191] Ross Caldwell, 'Enterprise goes into reverse for floating charge-holders' (2019) 1 Jur. Rev. 103-111, 108.
[192] DTI 2001 (n 135).
[193] Interviewee 1 (Credit Manager) (By phone, UK, 04 December 2018); see Appendix D.
[194] John Tribe, '"Policy subversion" in corporate insolvency: political science, Marxism and the role of power interests during the passage of insolvency legislation' (2019) 32 Insolv. Int. 59-66.

2.4.2.4 Employees

During a potential rescue the workforce will certainly be subject to certain changes. The information that the employees obtain during a subsequent rescue are limited thence, their input towards a successful rescue is restricted.[195] In other words, the staff's right to intervene or to express their opinion during rescue is diminutive and its contribution is minor to the turnaround of the company. Even if rescue fails the employees are in a more favourable position than unsecured creditors as they have a preferential status.[196] This occurs because the rights of the employees are perceived as more essential than the rights of unsecured creditors.[197] This is ethically acceptable and encouraged since it is viewed as a social benefit.[198] This can be traced back to the debate on preferential claims of the late 19th century.[199] It was contemplated that the raw materials are part of the debenture holder assets hence, their value should not be underestimated.[200] This is practically linked with the labour theory of value where employees add value to raw materials.[201] The return Crown's preferential status in insolvency will be ranked as a secondary preferential debt, which is a further reason to avoid floating charges.[202]

When shares of the company are sold to a new person it means that the entity is kept. The owner would be bound by their existing employment contracts due to Transfer

[195] Finch, 'Corporate rescue: Who is interested?' (n 131) 205.
[196] IA 1986, Sch 6, Category 5.
[197] The Insolvency Service, 'House of Commons Business and Enterprise Committee - Sixth Report of Session 2008-9' (2009) 11.
[198] Parry (n 131) 4.
[199] Preferential Payments in Bankruptcy Amendment Act 1897.
[200] Hansard, Parliamentary Debates, Preferential Payments in Bankruptcy Act (1888) Amendment Bill, HC Deb (10 February 1897) Series 4, Vol. 46 cc70-87.
[201] Jacques Delacroix 'The Export of Raw Materials and Economic Growth: A Cross-National Study' (1977) 42 American Sociological Review 795-808, 800.
[202] HM Treasure, 'Protecting your taxes in insolvency: Budget 2018 brief', 29 October 2018 <https://www.gov.uk/government/publications/protecting-your-taxes-in-insolvency-budget-2018-brief> accessed 3 August 2020.

of Undertakings (Protection of Employment) Regulations 2006 (TUPE). The employees might be asked to work in a different way than they used to, but this happens only if it is allowed by the employment contract that the employee signed.[203] The impact of transfer of TUPE is pertinent as in reality the Newco will not survive if the wages are not paid to the employees or if they are not well treated. TUPE generally protects the employees by ensuring that all employees are transferred in a company/business sale, but things can be different for insolvent companies.[204] If the buyers were forced to take on all of the workforce, rescue could be discouraged. The downsizing of a company while reorganising it will probably result in redundancies. During a rescue procedure an employee would welcome a trading rescue with the expectation of having his/her employment continued.[205] While the company is in administration, the IP ensures that their services are undertaken by paying them their salaries/wages in priority of others.[206]

As discussed in *Powdrill* a significant aspect of rescue culture is the preservation of the jobs of the company. The ultimate result though would be to recover the company in a way that its trading collaborations are protected and the majority of the employees are preserved.[207] However, this is not always the case since business and/or asset sales are the prevalent outcomes. The maintenance of some of the employment through a business sale is still a more favourable result than liquidation and the eventual loss of all jobs.[208] In a pre-pack sale and other business sales the company usually transfers its employees to the Newco under TUPE in which the employees are protected.[209] Even though the employment preservation is an essential part of rescue culture, the

[203] Belcher (n 4) 201.
[204] TUPE, r 8 and 9.
[205] Finch and Milman (n 8) 206.
[206] IA 1986 Sch 6, Category 5; Paul Davies, 'Employee Claims in Insolvency: Corporate Rescues and Preferential Claims' (1994) 23 ILJ 141-169, 144.
[207] Hansard (n 113).
[208] Carruthers and Halliday (n 1) 71.
[209] Ben Jones, Nicole Hallegua, 'Should an Administrator Consult?' (2010) 3 C.R. & I. 164-165.

legislation's purpose is to benefit creditors as a whole and the optimum way of achieving that more effectively is through business rescue.

2.5 Rescue finance for SMEs

SMEs are more susceptible to distress, as R3 reported that 37 per cent of small enterprises had their profits decreased while medium-sized enterprises reached a drop of 19 per cent and large enterprises profits decreased by 7 per cent.[210] Development linked with innovation is substantial in the SME sector. This is closely related with the theory of creative destruction that was mentioned earlier in this chapter. Yet, successful rescue outcomes encourage entrepreneurship and companies to take risks. This could include accessibility to procedures with less complicated provisions, limited costs and the formation of devices that would ease their financing. As SMEs are the lifeblood of the economy where their development is crucial, this section targets to determine the financing aspects that need further investigation.

The cash-flow of a distressed company is significantly low – if it even exists – therefore, the procurement of a funding source is a vital aspect of rescue as various costs will arise. There are arguably insufficient incentives to provide rescue finance in both the UK and Cyprus. This issue is reviewed through the standpoint of the UK and the United States of America (USA) in Chapters 4 and 6 respectively.[211] It seems that the USA Chapter 11 is more advanced in the sector of rescue finance. Also, the Directive (EU) 2019/1023 (the 2019 directive) has some provisions that address the issue of rescue

[210] R3, 'Business Distress Index' December 2012 <https://www.r3.org.uk/media/documents/policy/research_reports/bus_distress_index/R3_Business_Distress_Wave_9_FINAL.pdf> accessed 17 December 2019.
[211] See Chapter 4, Section 4.7 and Chapter 6, Section 6.2.3.

finance, but it is on the European Union member states to decide about the level of incentives that are provided to prospective financiers.

Credit can be raised through four main methods: providing security, unsecured loans, sale agreements that operate as 'security devices' and guarantees.[212] Security reduces the level of risk of the creditor and provides an enforcement power. Other benefits of security are that it obstructs other creditors from confiscating the secured assets and it also refrains from ranking *pari passu*. Unsecured loans are rarely chosen as priorities put unsecured creditors in a devastating position. The 'security devices' include amongst other things, retention of title, sale and repurchase contracts, factoring and invoice discounting agreements, and hire purchase agreements.[213] This is a method of retrieving finance by providing ownership to those assets. Parent or subsidiary companies are allowed to be guarantors, but an indemnity that would protect those guarantors can be given by the debtor company.[214] The assurance of returns to creditors is an essential attribute for securing debt finance, as they will otherwise not give their consent.[215]

The various means of retrieving finance are generating controversies that need to be balanced with the conceivable recommendations of altering the regime. The ICG Report 2018 interestingly stated that "rescue finance was a complex matter, and that it was wary of introducing changes that may have adverse effects on the general (non-distressed) lending market".[216] The existence of security and priority – as well as their combination – aids financing operations since if the circumstances were different

[212] Vanessa Finch, 'Security, Insolvency and Risk: Who Pays the Price' (1999) 62 M.L.R. 633-670.
[213] Ibid.
[214] Ibid.
[215] Rafael La Porta et.al, 'Legal Determinants of External Finance' (1997) 52 The Journal of Finance 1131.
[216] Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) (ICG Report 2018).

financing would be unattainable.[217] During the last thirty years there has been a gradual increase of asset-based lending, as it is now considered a conformist practice for several enterprises and principally SMEs.[218]

It is usually the floating charge holder who is funding a rescue process. The floating charge holder might not directly fund the process, but the expenses will be deducted from his/her assets.[219] The super-priority consideration that has been on the table for years is a discussion that fits here. Debtor-in-possession financing agreements in the USA are an exemplar method for incentivising lenders to provide credit while the company is on the verge of insolvency. Perhaps the embracement of the super-priority idea in the UK could become a catalyst for rescue outcomes. Banks are reluctant to approve the flow of further finance to be prioritised over their own existing debt.[220] Government reports/consultations have evaluated this aspect multiple times with the most recent being in 2016[221] and 2018.[222] The ICG Report 2018 highlighted that the UK jurisdiction is not yet ready for these unorthodox changes but clarifies that this issue will be revisited.

Floating charge assets are top-sliced by the prescribed part[223] and administration fees/expenses.[224] Preferential creditors are prioritised over all the aforementioned

[217] Steven Harris, Charles Mooney, 'A Property Based Theory of Security Interests: Taking Debtors' Choices Seriously' (1994) 80 Virginia Law Review 2021-2072, 2037.
[218] UK Finance, 'SME finance in the UK: past, present and future' December 2018 <https://www.ukfinance.org.uk/system/files/UK-Finance-SME-Finance-in-UK-AW-web.pdf> accessed 21 December 2019.
[219] Louise Gullifer, Jennifer Payne, *Corporate Finance Law: Principles and Policy* (2nd edn, Hart Publishing 2015) 305; the floating charge holder is usually the financier: Jennifer Payne, Janis Sarra, 'Tripping the Light Fantastic: A comparative analysis of the European Commission's proposals for new and interim financing of insolvent businesses ' (2018) International Insolvency Review 178.
[220] Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (EE Publishing 2008) 194-195.
[221] The Insolvency Service, A Review of the Corporate Insolvency Framework: A consultation on options for reform the Corporate Insolvency Framework response form (25 May 2016) (2016 Consultation).
[222] ICG Report 2018 (n 216).
[223] IA 1986, s 176A.
[224] IA 1986, s 176ZA.

categories (except from the administration fees/expenses) with the floating charge holders being ranked last. This statutory regime is prevailing at the expense of floating charge holders therefore, its fairness is arguably not balanced. The abolition of the Crown as a preferential creditor was a decision triggered post-EA 2002 that was supposedly done with the purpose of promoting justice.[225] The preservation of this preferential status of the HM Revenue and Customs (HMRC) would have been a detriment on unsecured creditors whose recovery prospects would have been diminished. The attempt to restore further justice to secured creditors happened through the prescribed part. Essentially, floating charge holders approved the contraction of their rights, in order to promote the greater good and to reinstate the integrity of the regime.[226] There have not been any indications that the position of unsecured creditors has been improved.[227] The return of the Crown preference[228] is thus expected to obstruct the procurement of finance thus, calls for reforms are anticipated.[229] This could be a further detriment to floating charge holders but also to unsecured creditors. Although the rise of the prescribed part cap has been promised to unsecured creditors, there are doubts as to whether this device is operating to their benefit.[230] All these are happening at the expense of floating charge holders as utilitarianism takes place. However, this further diminution of the rights of crucial players of rescue would demise the probabilities of having a successful corporate rescue.

[225] David Milman, 'Promoting distributional justice on corporate insolvency in the 21st century' in Jenny Steele, Willem Boom (ed.), *Mass Justice: Challenges of Representation and Distribution* (EE Publishing 2011) 171.
[226] Ibid.
[227] Also supported by Adrian Walters, 'Statutory Erosion of Secured Creditors' Rights: Some Insights from the United Kingdom' (2015) 2015 U Ill L Rev 543; see further about unsecured creditors in Chapter 2, Section 2.4.2.3 and Chapter 4, Section 4.2.2.
[228] HM Treasury, Budget 2018 (HMSO, 2018), HC Paper No.1629.
[229] Chris Umfreville, 'Pre-packaged administrations and company voluntary arrangements: the case for a holistic approach to reform' (2019) 30 I.C.C.L.R. 581-603.
[230] See Chapter 2, Section 2.4.2.3.

In the 1897 Act debates, it was argued that there should not be a differentiation between fixed and floating charges as it was an audacious move.[231] Hopkinson justified this through the labour theory of value, where he said that the employees contributed to the progress of the company hence, their priority should be preserved.[232] Mokal supports that as the fixed charge holder is at the top of the distribution ranking it is more possible to continue to finance the distressed company.[233] He said that this is encouraging rescue whereas floating charge holders could not give such a contribution. The case law that surrounds floating charges is also an impediment to the development of English personal property security law.[234] Litigation costs that are correlated to floating charges signify that it is somehow even more problematic.[235]

Floating charges are on a certain extent necessary for the structured insolvency regime of the UK to operate properly. The absence of a floating charge does not necessarily preclude payment of expenses due to the voluntary funding operation by fixed charges holders. The treatment of floating charge assets gave rise to a concern about the extent of the office-holder remuneration since it is extracted from floating charge assets.[236] Following this, the Kempson Report led to the initiation of fee estimates and expenses, which aimed at alleviating the potential unscrupulous acts of office-holders.[237] Without the floating charge assets several questions will arise such as: Should there be a priority of secured creditors over all stakeholders? What happens to the prescribed part and the preferential creditors? It is conceivable that this change

[231] Hansard, Parliamentary Debates (4th Series), 60 Vict., Vol XLVI (10 February 1897), 86 Col 2, 87 Col 1 (Sir Robert Findlay, Solicitor General).
[232] Ibid 83 Col 1 (Mr Alfred Hopkinson MP).
[233] Rizwaan Mokal, *Corporate Insolvency Law: Theory and Application* (OUP 2005) 202-208.
[234] Ewan McKendrick, *Goode on Commercial Law* (5th edn, Penguin 2016) 766.
[235] See Chapter 4, Section 4.3 for this.
[236] Office of Fair Trading, *The Market for Corporate Insolvency Practitioners* (OFT 2010).
[237] Elaine Kempson, 'Review of Insolvency Practitioners Fees: Report to the Insolvency Service' (July 2013) < https://www.gov.uk/government/publications/insolvency-practitioner-fees-a-review> accessed 4 October 2019.

will hinder the system rather than promote rescue, as impediments regarding the maintenance of balance will evolve. Frisby reinforces this view by highlighting that: "To the extent that the entirety of the corporate estate is covered by what is or resembles fixed-charge security, it may be that insolvency practitioners find the task of formulating and pursuing a rescue outcome somewhat more Byzantine than in different times".[238]

The rise of these 'security devices' became more mainstream after the introduction of the EA 2002 and *Re Spectrum Plus Ltd.*[239] In *Spectrum* there was a restriction of the instances where security over receivables would be classified as fixed charges. Even pre-*Spectrum*, Worthington pinpointed that only in limited circumstances there can be a fixed charge over receivables.[240] Armour suggested this will lead to the upsurge of factoring agreements.[241] Lenders found a way to overcome and minimise the problems surrounding the *Spectrum case* through following devices that lead to invoice discounting and factoring agreements.[242] This has been an attractive option for SMEs as it mitigates the financing costs and may aid them to grow.[243] The effect is not the same though in the plight of insolvency.

The costs of retrieving security coupled with litigation costs also incentivised the development of asset-based finance.[244] If the security of creditors is subject to floating charges, the costs are repelling creditors from lending.[245] Milman suggests that

[238] Sandra Frisby, 'Not quite warp factor 2 yet? The Enterprise Act and corporate insolvency (Part 1).' (2007) 22 B.J.I.B. & F.L. 327-331.
[239] [2005] UKHL 41.
[240] Sarah Worthington, 'An 'Unsatisfactory Area of the Law' — Fixed and Floating Charges Yet Again' (2004) 1 International Corporate Rescue 175, 182.
[241] John Armour, 'Should We Redistribute in Insolvency?' in Joshua Getzler and Jennifer Payne (ed.), *Company Charges: Spectrum and beyond* (OUP 2006) Chapter 9.
[242] Walters (n 227).
[243] Frisby, 'Not quite warp factor 2 yet? (Part 1)' (n 238).
[244] Armour (n 241).
[245] Ibid.

the costs could be reduced by exploiting technological developments.[246] The price of these asset-based lending is more accessible than the traditional overdrafting method.[247] Armour vigorously expressed that: "[t]he history of this litigation is that of sophisticated creditors seeking to adjust their affairs so as to fall outside the ambit of the statutory scheme".[248] Asset-based financing is not subject to the priorities thus, the returns are not affected by the ranking distribution.[249] Walton in consideration of some reforms on this matter he is suggesting that debt factoring agreement should be treated as a floating charge security.[250] In this way debt factors will not be treated in priority thus, more assets will be available for distribution to other stakeholders that are now disadvantaged.

The Law Commission of England and Wales initiated some consultations,[251] that had as a purpose to introduce reforms equivalent to functional security position of the USA Uniform Commercial Code Article 9 and the Personal Property Securities Acts of countries like New Zealand and Canada. One of the recommendations goes back to the elimination of the discrepancy between fixed and floating charges. Although the model of New Zealand was proposed in dealing with the impediments regarding redistributive provisions with this change, in the final report they decided to not trigger these amendments.[252] With the exception of the amendments to Companies Act 2006,

[246] Milman, 'Promoting distributional justice on corporate insolvency in the 21st century' (n 225).
[247] Walters (n 227).
[248] Armour (n 241).
[249] Sandra Frisby, 'Of rights and rescue: a curious confluence?' (2019) Journal of Corporate Law Studies <https://www.tandfonline.com/doi/pdf/10.1080/14735970.2019.1615165?casa_token=6utFTENN-j8AAAAA:6Rfb7XRQ3-1G3boYCP-A6lxraRtFLFdzpaPWI1X2RL9cvOBLaLMgaVBiuddu9nMj8Bhk4DNcBqRL> accessed 17 December 2019.
[250] Peter Walton, 'Fixed and floating charges: the Great British Fund-Off?' (2015) 1 JIBFL 3, 6.
[251] Law Commission, *Registration of Security Interests: Company Charges and Property other than Land* (Law Com No 164, 2002); Law Commission, *Company Security Interests: A Consultative Report* (Law Com No 176, 2004); Law Commission, *Company Security Interests* (Law Com No 296, 2005) (LC CP 296).
[252] Ibid LC CP 296, paras 3.171-3.175.

Part 25 and the restriction of not allowing assignment of receivables in business contracts, there were no other changes that followed the Commission Consultations.

Asset-based lending is more predictable, and creditors view it in a way that safeguards them from deficient practices of repayment.[253] Is this orientation enhancing rescue though? This could diminish the chances of the company being saved, as without the necessary incentive those financiers could easily cease the financing deftly.[254] With the return of the Crown preference the further increase of asset-based lending is expected. This will have as a consequence the extensive fragmentation of the company assets.[255] This fragmentation makes the restructuring plan more difficult for the administrator thus, this is discouraging rescue. Arguably, the floating charge holders will increase the interest rates[256] and a hesitation to provide funding is projected. The absence of super-priority and other possible incentives are likely to deteriorate the rescue outcomes.[257] The 2016 Consultation contained the valiant recommendation about changing the priorities of creditor classes in a way that would encourage rescue finance.[258] After the return of the HMRC preferential status, there should be calls for evaluations that would balance the interests of the main stakeholders and take into consideration the influence towards the national economy.[259] There should be an infrastructure that provides incentives that are harmonised with accountability and fairness.[260]

[253] Frisby, 'Of rights and rescue: a curious confluence?' (n 249); UK Finance (n 218).
[254] Frisby, 'Not quite warp factor 2 yet? (Part 1)' (n 238).
[255] Armour (n 242).
[256] Vanessa Finch, 'Re-invigorating corporate rescue' [2003] J.B.L. 527-557, 531.
[257] For further on super-priority see Chapter 4, Section 4.7 and Chapter 6, Section 6.2.3.
[258] 2016 Consultation (n 221).
[259] Ibid.
[260] Finch and Milman (n 8) 55-56.

2.6 Conclusion

This chapter is the baseline for the subsequent chapters that follow. The main target is to identify a procedure that would operate in an optimum level in both the UK and Cyprus. The use of the UK academic work, legislation and case law is valuable for identifying the limitations that could arise as well as the solutions. The issue of whether to pursue a company rescue or a business rescue is still controversial. Arguably, the matter is seen differently in each jurisdiction since diverging incentives are provided. Yet, this chapter is advocating that business rescue is an easier task that could balance the interests of stakeholders. The cooperation of the stakeholders before and while the company is in a formal rescue procedure is vital since this could determine the rescue outcome. The next two chapters illustrate the functioning as well as the limitations of the main procedures in the UK, as this is substantial for the deductions of this thesis. An issue that is accentuated in Chapter 5 is that only company rescue can be attained through the Cypriot examinership. That said, the Cypriot regime that is creditor controlled to a certain extent will possibly not welcome this procedure. This justifies the inclusion of the USA Chapter 11 in the analysis since the rehabilitation of the entity through that mechanism is not a peculiar phenomenon.

Chapter 3 – Company Voluntary Arrangements

3.1 Introduction

Company Voluntary Arrangements (CVAs) are binding compromises or arrangements between the company and company creditors, whereby, amongst other things, debts are allowed to be repaid in instalments.[1] CVAs have the form of statutory contracts that give rise to questions of contractual interpretation.[2] The initial aim of CVAs was to be used as a rescue tool for companies but now it is occasionally used because it facilitates a softer entry into liquidation.[3] CVAs[4] as well as administrations[5] that were introduced under the Insolvency Act 1986 (IA 1986) came out of the recommendations of the Cork Committee that had as a main target the incorporation of rescue culture in the jurisdiction.[6]

In 1991, there were 137 CVAs in England and Wales and by 1997 there was an increase to 629.[7] The uptrend continued and in 2004, 726 CVAs were recorded.[8] The Insolvency Service in 2012 documented the highest number of CVAs, which was 829.[9] By 2019 the number dropped to 351 CVA cases.[10] The Insolvency Service statistics point out that CVAs have never reached more than a thousand, which is disappointing

[1] Insolvency (England and Wales) Rules 2016 (IR 2016), r 2.3; *Re Arthur Rathbone Kitchens Limited* [1998] BPIR 683.
[2] *Simpson v. Bowker* [2007] EWCA Civ 772; *Re SHB Realisations Ltd (formerly BHS Ltd) (in Liquidation), Wright v. Prudential Assurance Co Ltd* [2018] EWHC 402 (Ch).
[3] David Milman, *Governance of Distressed Firms* (EE Publishing 2013) 18; Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (EE Publishing 2008) 76.
[4] IA 1986, Pt 1.
[5] See Chapter 4.
[6] Report of the Review Committee on Insolvency Law and Practice (Cmnd 8558, 1982) (Cork Report); See more about rescue culture in Chapter 2, Section 2.2.
[7] The Insolvency Service Statistics (Company Insolvency Statistics: October to December 2013), <https://www.gov.uk/government/statistics/insolvency-statistics-october-to-december-2013> accessed 25 October 2019.
[8] Ibid.
[9] The Insolvency Service Statistics (Company Insolvency Statistics: October to December 2019), <https://www.gov.uk/government/statistics/company-insolvency-statistics-april-to-june-2019> accessed 19 February 2020.
[10] Ibid.

considering that the number of corporate insolvencies is always more than 14,000.[11] CVAs are outnumbered by other insolvency procedures such as the modernised administration. Although CVAs are modelled after Individual Voluntary Arrangements (IVAs), unconventionally IVAs have been successful and a preferable option for personal insolvencies.[12] Therefore, the reasons that CVAs are seemingly less appealing are discussed.

CVAs are available to companies that are insolvent but not terminally insolvent.[13] 2018 was characterised as the year of CVAs, due to the attention that derived from retail and high street restaurants[14] such as New Look, Carpetright, Kingfisher, Prezzo, Byron Burger, Moss Bros and House of Fraser.[15] There have been indications that one of the main reasons that affected the performance of high street companies, is the extensive availability of online shopping.[16] Disputes between landlords and retailers/restaurateurs emerged as a result of these CVAs, which necessitates an analysis.[17]

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[11] The Insolvency Service Statistics 2019 (n 9).
[12] David Milman, 'Corporate insolvency in 2015: the ever-changing legal landscape' (2015) 369 Co. L.N. 1-5; For more about IVAs see Adrian Walters, 'Individual Voluntary Arrangements: A 'Fresh Start' for Salaried Consumer Debtors in England and Wales?' (2009) 18 I.I.R. 5-36 and David Milman, 'Personal Insolvency Law and the Challenges of a Dynamic, Enterprise-Driven Economy.' (2008) 20 SAcLJ 438-463.
[13] IA 1986, s 1(1); Kristin Van Zwieten, *Goode on Principles of Corporate Insolvency Law* (5th edn, Sweet & Maxwell 2019) 588.
[14] James Child, Pui-Guan Man, 'Retail in crisis: the story so far…' 25 October 2018 <https://www.egi.co.uk/news/retailcrisis/> accessed 29 October 2019.
[15] Sarah Butler 'Carpetright, Moss Bros, Kingfisher and New Look hit by retail woes' 21 March 2018 <https://www.theguardian.com/business/2018/mar/21/carpetright-moss-bros-kingfisher-high-street-retail-mothercare> accessed 03 November 2019; Elias Jahshan, 'House of Fraser settles landlords' legal challenge' 06 August 2018 <https://www.retailgazette.co.uk/blog/2018/08/house-of-fraser-landlords-legal-challenge-cva-settled/> accessed 03 November 2019.
[16] John Wood, 'M&S delivers – but is it too late?' June 2017 <https://theconversation.com/mands-delivers-but-is-it-too-late-79065> accessed 18 February 2020.
[17] See Chapter 3, Section 3.7.

Debtor-in-possession (DIP) is a crucial feature of CVAs since the directors maintain their managerial position.[18] Even though directors retain their management powers, a supervisor[19] is appointed who forms the arrangement between the company and its creditors. The DIP feature can produce both favourable and negative outcomes, but this also depends from the lens that you are seeing it from.[20] CVAs are interchangeably used with administration as an exit procedure for different strategy purposes. Through twinning CVAs with administration, the DIP characteristic is not in effect.[21]

Critics thought that the underperformance of CVA happened because a moratorium was unavailable.[22] This led to the initiation of a CVA with a moratorium through the Insolvency Act 2000.[23] Currently, the benefits of this new-style CVA are still questionable. The statistics suggest that CVAs are underused[24] thus, one could assume that it is an inefficient mechanism. Yet, a recent report[25] has suggested that CVAs can be successful and that the ultimate task is to identify a strategy that would make this process more attractive.

[18] Ian Fletcher, 'UK Corporate Rescue: Recent Developments — Changes to Administrative Receiverships, Administration Company Voluntary Arrangements — The Insolvency Act 2000, The White Paper 2001 and the Enterprise Act 2002' (2004) 5 E.B.O.R. 119.
[19] A licenced insolvency practitioner (IP).
[20] Further analysis on DIP benefits and drawbacks can be found in Chapter 6, Section 6.2.1.
[21] Gerard McCormack, Wai Yee Wan, 'Transplanting Chapter 11 of the US Bankruptcy Code into Singapore's restructuring and insolvency laws: opportunities and challenges' (2019) 19 Journal of Corporate Law Studies 69–104.
[22] Andrew Keay, Peter Walton, *Insolvency Law: Corporate and Personal* (4th edn, Jordan Publishing 2017) 139.
[23] IA 1986, Sch A1.
[24] The Insolvency Service Statistics 2019 (n 9).
[25] Peter Walton, Chris Umfreville, Lézelle Jacobs, 'Company Voluntary Arrangements: Evaluating Success and Failure' R3: Association of Business Recovery Professionals, May 2018).

3.2 Purpose

According to the Cork Report, the initiation of CVAs had the purpose to facilitate the rescue of a distressed entity. In comparison to other insolvency processes the guidance on CVAs is not detailed therefore, a CVA proposal implementation can be flexible.[26] The purpose and guidance on CVAs are not entirely contained in the legislation thus, this vastly depends on case law.[27] Arguably, the purpose of CVAs can be gleaned from IA 1986, s 1(2) which states that: "The directors of a company may make a proposal under this Part to the company and to its creditors for a composition in satisfaction of its debts or a scheme of arrangement of its affairs". This is a broad purpose and is not as specific as the administration objectives.[28] If the directors have extensively invested in their business, they might hesitate to take this step. The threat and current use of wrongful trading law is arguably not enough.[29]

CVAs can be used to attain a composition of owed debts, which means the "writing off of a proportion of their debt"[30] or to create a scheme of arrangement.[31] The composition of debts facilitates the devaluation of the owed debt to creditors and establishes the binding nature of this agreement as it even binds the dissentient creditors.[32] Schemes of arrangement (SoAs) are structured in a way that the creditors receive their returns in full but not instantly. In situations where the creditor is interested to the company, the scheme can take the form of a debt-equity swap.[33] That said,

[26] Sandra Frisby, 'Insolvency Law and Insolvency Practice: Principles and Pragmatism Diverge?' (2011) 64 Current Legal Problems 349-397.
[27] Keay and Walton, *Insolvency Law* (n 22) 139.
[28] For the hierarchical objects see Chapter 4, Section 4.2.
[29] IA 1986, s 214; *Re Ralls Builders Ltd (in liquidation); Grant and another v. Ralls and others* [2016] EWHC 1812 (Ch).
[30] *Inland Revenue Commissioners v. Adam & Partners Ltd* [2001] 1 BCLC 222.
[31] Keay and Walton, *Insolvency Law* (n 22) 140.
[32] Ibid.
[33] Ibid.

although the above can be applied in a CVA plan separately,[34] the plan can also defer a payment of a debt with the combination of reducing the debt burden.

During a CVA, a company can continue trading by agreeing to provide monthly instalments to creditors, but this could endure for years as the statutory deadline for CVAs is non-existent.[35] An empirical research showed that the dividends to creditors can increase when the procedure lasts longer.[36] However, it was in tandem recommended that CVAs should not last for longer than three years, excluding special circumstances. In *Re NT Gallagher & Son Ltd,*[37] it was stated that "the primary purpose of the CVA was to enable Gallagher to go on trading". Roger Kaye QC in *Re Arthur* argued that "[t]he purpose of the CVA was to enable the company to trade out of its insolvency and make provision for creditors by stage payments...." CVAs can aid a company restructuring since it could focus on a specific class of creditors that potentially endanger the continuation of company trading.[38]

The initiation of a CVA is not entirely focused on company rescue since it functions as a tool that facilitates the realisation of assets, which could have a simpler method than rescue.[39] Yet, it is (or it can) in itself (be) a self-evident corporate rescue procedure since the company character and management does not change. The interests of creditors are always considered since the procedure will only have a prospect if the main creditors support it. Supervisors often conduct CVAs with the aim of asset

[34] *March Estates Plc v. Gunmark* [1996] 2 BCLC 1.
[35] Ibid; Adrian Walters, Sandra Frisby, 'Preliminary Report to the Insolvency Service into Outcomes in Company Voluntary Arrangements' (2011) SSRN <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1792402> accessed 05 December 2019.
[36] Walton, Umfreville and Jacobs (n 25) 31.
[37] [2002] 2 BCLC 133.
[38] Pension Protection Fund 'Company voluntary arrangements: PPF Restructuring & Insolvency Team – Guidance Note 5' December 2018 <https://www.ppf.co.uk/sites/default/files/2019-01/company_voluntary_arrangements_ri_guidance_note_5.pdf> accessed 25 September 2019.
[39] Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 424; Van Zwieten (n 13) 599.

realisation thus, the perception that CVA is an alternative to liquidation originates by the particular usage.[40] This function is identified in *Oakley-Smith v. Greenberg,*[41] in which it was suggested that CVAs are more suitable than administration when it comes to creditor distribution. *Greenberg* though precedes the enforcement of the EA 2002 amendments which means that this approach is possibly not accurate anymore.[42]

A CVA can even be proposed after a liquidator has been appointed.[43] When the final target is to realise the assets and then liquidate the company, this does not have to take place instantly. A trading CVA and a more organised liquidation could produce better results for all stakeholders and particularly for creditors. The breadth of liquidator's powers is extended if s/he also manages the CVA of the company, which would address hurdles regarding trading. When directors do not want to lose control over the company, they choose to follow a CVA, which could come into conflict with the protection of creditor's interests.[44]

3.3 Challenges regarding the CVA procedure

3.3.1 Initial Steps and Proposal

The director occasionally fails to take effective measures (i.e. enter a rescue plan) on time since the company might already be in a financially irreversible position. This possibly happens because the officers of the company omit to recognise on time that the

[40] John Tribe, 'Company voluntary arrangements and rescue: a new hope and a Tudor orthodoxy' (2009) 5 J.B.L. 454-487.
[41] [2002] EWCA Civ 1217.
[42] Tribe (n 40).
[43] IA 1986, s 1(3)(b).
[44] Walton, Umfreville and Jacobs (n 25) 56-57; Further about the effectiveness of CVA can be found in Chapter 3, Section 3.5.

company is in trouble.[45] The director must recognise and accept that the company is in economic hardship and identify whether there is a legitimate prospect of survival. When the company has limited possibilities of being saved, it is more appropriate to wind up the company rather than diminishing the company value. It was expected that companies would only use CVAs if it did not worsen the situation of creditors in comparison to liquidation.[46] The nominee has the duty of orchestrating the optimum scheme through gathering information regarding the economic position of the company, current business assets and liabilities, and cash-flow.[47]

Commonly a proposal is created by the directors of the company or by the administrator when the company is in administration.[48] Less commonly, a proposal is initiated by the liquidator when the company is in liquidation.[49] The nominee who is appointed by the director has an oversight role regarding the proposal and the director is accountable for providing the needed information to the nominee. In *Cooper v. Fearnly,*[50] it was stated that the nominee is responsible for determining whether the proposal is "serious and viable". The proposal must be submitted to the court by the nominee within 28 days of the proposal's notice.[51] The role of the judiciary in a CVA is usually administrative since the control regarding decisions is mainly on creditors but simultaneously directors have some minor responsibilities.[52] The court has the authority

[45] Mark Phillips, Jeremy Goldring, 'Rescue and reconstruction' (2002) 15 Insolv. Int. 75-78; John Armour, Audrey Hsu, Adrian Walters, 'The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings' (December 2006) Insolvency Service Report, 22.
[46] Rebecca Parry, *Corporate Rescue* (Sweet & Maxwell 2008) 157.
[47] Van Zwieten (n 13) 592-593.
[48] IA 1986, s 1(3).
[49] *Re Greystoke* [1996] 2 BCLC 429; IA 1986, s 1(1), s 1(3).
[50] [1997] BPIR 20.
[51] IA 1986, s 2(2)(a).
[52] Parry (n 46) 171.

though to resolve disputes for issues that relate to unfair prejudice and/or material irregularity.[53]

3.3.2 Meetings

The proposal should be approved by a company meeting, which requires the approval of 50 per cent of the company shareholders[54] and by a creditors' meeting that needs more than 75 per cent in value of debt consent votes by unsecured creditors.[55] The purpose of the meetings is to decide whether to approve the proposed arrangement with or without alterations.[56] The fact that it is not possible to produce a proposal where unsecured creditors will be treated equally – due to *pari passu* – is arguably a constraint.[57] However, the *pari passu* rule was arguably infringed in *BHS*.[58] If the CVA obtains the necessary majorities it is approved and automatically binding to all unsecured creditors, regardless of the circumstances.[59] The arrangement is not binding on secured and preferential creditors[60] but if their interests are negatively affected they may intervene.[61] For instance, if secured creditors are restricted from enforcing their security, the proposal will not take effect.[62]

[53] See Chapter 3, Section 3.3.3.
[54] IR 2016, r 2.36.
[55] IR 2016, r 15.34(3); Following the Small Business, Enterprise and Employment Act 2015 new decision procedures apply. For this see IA 1986, s 4(6A).
[56] IA 1986, s 4(3), s 4(4).
[57] *Re Courts Plc (In Liquidation)* [2008] EWHC 2339 (Ch); [2009] 1 W.L.R. 1499; Rizwaan Mokal, 'Priority as pathology: the pari passu myth' (2001) 60 C.L.J. 581-621.
[58] Helen Coverdale, Joanna Froy, 'A victory for landlords? A look at Wright & Anor (Liquidators of SHB Realisations Ltd) v The Prudential Assurance Company Ltd [2018] EWHC 402 (Ch)' (2018) 11 C.R. & I. 89-91; see a further analysis of the case in Chapter 3, Section 3.7.
[59] *Beverley Group Plc v. Mc Clue* [1995] 2 BCLC 407.
[60] IA 1986, s 4(3).
[61] IA 1986, s 4(4).
[62] IA 1986, s 5.

3.3.3 Challenging the Arrangement

The CVA meeting decision may be challenged on the grounds of unfair prejudice[63] or material irregularity.[64] The ground of unfair prejudice is only enforced when there is a different treatment towards a particular creditor in comparison to other creditors.[65] Unsecured creditors are not discrete in "classes" and this is potentially creating problems. In theory, the treatment towards unsecured should be equal, which is arguably unfair. Although equal treatment applies to all unsecured creditors, occasionally commercial criteria distinguishes the creditors into groups.[66] There have been disputes between landlords and retailers about the fairness of CVAs because landlords are usually crammed down. It is argued that while other creditors are paid in full, landlords fees are reduced, which limits their returns.[67] Etherton J dealt with this issue of landlords and whether they suffered unfair prejudice in *Prudential Assurance Co Ltd v. PRG Powerhouse Ltd.*[68] It was held that if the company was liquidated the landlords would have been in a better position hence, the court ruled that there was indeed an unfair prejudice, but it was also mentioned that each case must be decided in accordance with the unique occurrences of the case. The *Mourant & Co Trustees v. Sixty (UK) Ltd*[69]followed the decision of *Powerhouse,* but it was also stated that the possibility of having a successful challenge on the ground of unfair prejudice is slim. Most challenges fail because the collective interest prevails over the interest of individuals.[70] According

[63] IA 1986, s 6(1)(a) and Sch A1 para 38(1)(a).
[64] IA 1986, s 6(1) (b) and Sch A1 para 38(1)(b).
[65] Karia Pranai, Ross Miller, 'Company voluntary arrangements - the landlord's position' (2003) 19 I.L. & P. 87-89.
[66] David Milman, 'The rise of the objective concept of "unfairness" in UK company law' (2010) 286 Co. L.N. 1-4.
[67] See Chapter 3, Section 3.7; For further see *Discovery (Northampton) Ltd and others v. Debenhams Retail Ltd and others* [2019] EWHC 2441 (Ch).
[68] [2007] Bus LR 1771.
[69] [2010] EWHC 1890.
[70] *Swindon Town Properties Ltd v. Swindon Town Football Co Ltd* [2003] BPIR 253 Ch D; *SISU Capital Fund Ltd v. Tucker* [2005] EWHC 2170 (Ch).

to Milman: "there is a clear potential for the criterion of unfairness to be invoked in order to challenge CVAs, but it is only in an extreme case that such a challenge will prove successful."[71] The analogous unfairness challenges in administration can be initiated through the IA 1986, Sch B1, para 74, which is currently experiencing a high failure rate.[72]

Material irregularity requires an irregularity and simultaneously be of substance.[73] Matters of substance are for instance, a vote that was not taken into account by the chairman;[74] a notice that was never received by a creditor who provided a substantial amount of credit;[75] when a falsehood is triggered;[76] when information was not fully disclosed during the meeting.[77] Evidence must be provided that would prove that this irregularity impacted the arrangement to the extent that the outcome would have been different.[78] It is common for irregularities to take place during a meeting thus, the applicant must be mindful of the materiality of the incident. If the court states that any of these two grounds have emerged, the CVA may be revoked or suspended and the court will order the summoning of the meetings to review again the proposal.[79]

[71] Milman, 'The rise of the objective concept' (n 66).
[72] *Davey v. Money* [2018] EWHC 766 (Ch); for further see Chapter 5, Section 5.5.2.
[73] Shearman & Sterling LLP, Corporate insolvency: company voluntary arrangements - Re Portsmouth City Football Club (In Administration)' (2010) 25 J.I.B.L.R. N143-144.
[74] *Re a Debtor (No.222 of 1990), ex parte Bank of Ireland* [1992] BCLC 137, 146.
[75] *Re a Debtor (No 259 of 1990)* [1992] 1 All ER 641, 644.
[76] *Re a Debtor (No.87 of 1993) (No.2)* [1996] BCC 80; IA 1986, s 262 which is the analogous IVA provision.
[77] *Somji v. Cadbury Schweppes Plc* [2001] 1 WLR 615; IA 1986, s 262(1) which is the analogous IVA provision.
[78] Parry (n 46) 195.
[79] IA 1986, s 6(4).

3.3.4 Implementing and Terminating the Arrangement

After the scheme is approved the nominee is appointed as a supervisor[80] and s/he is the person who implements the arrangement. The nominee – who is also an IP – should be in the position to determine whether the arrangement has "a reasonable prospect of being approved and implemented" before an official submission at court.[81] If any creditor is unpleased with the supervisor's action, the creditor may apply to the court, which could change, reverse or approve the supervisor's decisions.[82] A CVA may be terminated because the time of the agreement lapses or the debtor could not keep up with the payments to creditors or because the required payments have been paid earlier. Yet, the most common result of CVAs is liquidation. This exit scheme raises some issues. Is the CVA terminated after the company enters liquidation or does it continue? Is the control of the company transferred from supervisor to the liquidator? In *Re NT Gallagher & Son Ltd* it was stated that these issues should be determined before the agreement takes place thence, the CVA terms should provide those answers.

3.4 CVA with a moratorium

Consultative papers of the Insolvency Service suggested that one of the main restrictions of the original CVA was the absence of a moratorium.[83] These suggestions led to the IA 2000, which introduced a CVA with a moratorium. The moratorium was designed to help small companies recover from their pecuniary problems by giving them the breathing space to organise a workout.[84] The new CVA aimed to deal with the

[80] IA 1986, s 7(2) and Sch A1, para 39(2).
[81] IR 2016, r 2.9(2).
[82] IA 1986, s 7(3) and Sch A1 para 39(3), (4); *Holdenhurst Securities Plc v. Cohen* [2001] 1 BCLC 460.
[83] The Insolvency Service, 'Company Voluntary Arrangements and Administration Orders: A Consultative Document' (October 1993); Revised Proposals for a New Company Voluntary Arrangement Procedure: A Consultative Document, (April 1995).
[84] Lynn Hiestand, Christian Pilkington 'CVAs – a restructuring tool for the future?' Recovery (2006) 18.

old CVA limitations, but the latest studies indicate that it is much more underutilised than the old type.[85] This new moratorium was arguably introduced for the benefit of small companies entering a CVA, but one wonders whether much of this avail exists in reality since companies barely use it. Commonly companies choose to enter the old style CVA instead of the new style.[86]

This moratorium gives 28 days of protection to the company, that includes the possibility of extending it for another two months.[87] The operation of the procedure remains mostly the same since a director stays at his/her position and the IP deals with the affairs of the procedure.[88] The director along with the IP must discuss whether the company passes the eligibility criteria for entering a CVA with a moratorium.[89] A company is eligible only if two or more of the following criteria are satisfied: the turnover of the company is not beyond £10,2 million per annum, the employees were less than 50, or the balance sheet total was not more than £5,1 million per annum.[90] Contrariwise, it appears that the cost of the new CVA procedure is higher than the old style CVA. Although CVA with a moratorium was designed for smaller companies, high expenses are obstructing them from using the proves.[91] CVA with a moratorium could be more useful to larger companies but access is restricted to them. With this CVA type being inaccessible to larger companies, they are driven towards the path of administration.[92]

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[85] Walton, Umfreville and Jacobs (n 25) 17; Walters and Frisby (n 35); David Milman, 'Moratoria in UK insolvency law: policy and practical implications' (2012) 317 Co. L.N. 1-4.
[86] Walters and Frisby (n 35); Walton, Umfreville and Jacobs (n 25) 17.
[87] IA 1986, Sch A1, para 32.
[88] Leanne Tilbrook, 'Corporate Rescue Reform in the UK' (2000) 2 J.I.F.M. 65-69.
[89] David Marks, 'Insolvency Act 2000: the practitioner's exposure to the cold winds of the moratorium' (2003) 16 Insolv. Int. 57-59.
[90] Companies Act 2006 (CA 2006), s 382(3).
[91] David Milman, Francis Chittenden, *Corporate rescue: CVAs and the challenge of small companies* (Chartered Association of Certified Accountants 1995); Finch and Milman (n 39) 425.
[92] Walton, Umfreville and Jacobs (n 25).

Criteria are not limited to the size of the company since a moratorium cannot be sought if it is an insurance company or a bank; if it has already been in an insolvency procedure; if it has been protected by another moratorium in the previous 12 months; if it was under administration in the last 12 months. CVA with a moratorium – as it necessitates transparency – all business documents of the company must state that the company is in a CVA,[93] which could drive away customers and weaken any prospect of future trading.[94] This can stigmatise the company and concurrently lead to a more costly and complex procedure.[95] The arduous supervisor duties are also making CVA with a moratorium more unappealing.[96] It has been characterised as a "dismal failure"[97] therefore, this mechanism is an encumbrance to the insolvency regime. The intention of implementing the CVA with a moratorium might have been genuine, but due to the usage thresholds impediments are generated for most companies that could have a legitimate interest in using it.[98]

3.5 How successful is a CVA as a rescue process?

In the face of changes to the CVA regime, including those introduced by the IA 2000, yearly statistics since 2011 have shown a steady decline in the use of CVAs. In 2012 and 2014 the number of CVAs reached 829 and 559 respectively, which means that there was a huge drop by 2019 since only 351 CVAs took place.[99] There are various

[93] IA 1986, Sch A1, para. 16.
[94] Brenda Hannigan, *Company Law* (4th edn, OUP 2012) 571.
[95] Chris Umfreville, 'A review of the corporate insolvency framework: a new moratorium to help business rescue?' (2016) 385 Co. L.N. 1-4.
[96] Gerard McCormack, 'Rescuing small businesses: designing an "efficient" legal regime (2009) 4 J.B.L. 299-330.
[97] Milman, 'Moratoria in UK insolvency law' (n 85).
[98] Jennifer Payne, 'Debt Restructuring in the UK' (2018) 15 European Company and Financial Law Review 449–471, 453.
[99] Insolvency Service Statistics 2019 (n 9).

factors that have potentially contributed to the downfall of the CVA usage. Even though CVAs are not that appealing it would be interesting to observe the outcomes of this process to establish whether this mechanism can be effective. It is indispensable to have realistic expectation to have a viable outcome.[100]

Walton, Umfreville and Jacobs studied some CVA cases that had the following outcomes: 65.2 per cent were terminated, 16.3 per cent are ongoing and 18.5 per cent were implemented.[101] The implemented CVAs are divided as follows: survival (12.3 per cent), immediate insolvency (3.6 per cent) and later insolvency (2.5 per cent).[102] This shows that an implemented CVA does not necessarily result in rescue. There is not a major divergence from the empirical research of 2011 since only the 10 per cent of companies continued trading after the CVA was completed.[103] Various thresholds need to be satisfied for a rescue to be achieved in a CVA hence, the most conventional outcome is liquidation. However, if a realistic and viable plan is triggered, rescue within a CVA would be possible. A CVA has the capacity of restoring the company by bringing it back into profitable trading.[104]

When the company is struggling financially, the debtor might not yet be ready to accept defeat or failure.[105] It is difficult to take an objective view, since they do not realise that initiating an insolvency scheme at the right time might prove to be advantageous and not result in a company failure. This is only likely to occur at the smaller end of the market but in any event, a director should seek advice when a company is driven to insolvency. That said, it would be beneficial to construct some

[100] Keay and Walton, *Insolvency Law* (n 22) 151.
[101] Walton, Umfreville and Jacobs (n 25) 12.
[102] Ibid.
[103] Walters and Frisby (n 35).
[104] Van Zwieten (n 13) 599-600.
[105] Tim Mocroft, 'Companies cannot do it alone: An investigation into UK management attitudes to Company Voluntary Arrangements' (CSFI, 2004).

devices that would facilitate the necessary awareness to directors. The DIP feature of CVAs might not be enough to incentivise the director to take action before the company is an irreversible.[106] Wrongful trading could potentially discourage directors from not pursuing a solution but these rules are not viewed as that effective.[107] Besides, it could be argued that if the insolvency is filed at a late stage, where the financial plight of the company is worsening, the creditor would put the company into liquidation. This is likely to affect smaller companies where owners are also the directors of the company.

Most creditors are in good terms with CVAs since they receive better returns than in liquidation. Yet, ordinarily the creditors opt for administration – although this would depend on the creditor type – because the management falls in the hands of the administrator.[108] Creditors believe that through having an increased control, their returns would be better. Sometimes though, directors could also be the creditors or the shareholders of the company hence, they often have a pecuniary interest in the success of the CVA. The creditors might view administrations as more trustworthy because the objectives that are pursued in administration are more straightforward.[109] This also occurs because a company might be financially troubled due to the mismanagement, which will prospectively carry on after the CVA.[110]

Creditors prefer procedures in which they are in more control since they have an intense suspicion that phoenix company activity might be in progress.[111] These

[106] Milman, *Governance of Distressed Firms* (n 3).
[107] IA 1986 s 214; see Chapter 2, Sections 2.2. and 2.4.2.2, Chapter 5, Section 5.5.2. and Chapter 6, Section 6.2.1.
[108] Mark Phillips, Jeremy Goldring, 'Rescue and reconstruction' (2002) 15 Insolv. Int. 75-78; see Chapter 2, Section 2.4.2.1.
[109] IA 1986, Sch B1, para 3.
[110] Gary Cook et al., 'Small Business Rescue: A Multi-Method Empirical Study of Company Voluntary Arrangements' (2003) ICAEW,London.
[111] Chris Umfreville, 'Taking a DIP into the pool: should the Pre-Pack Pool be extended to CVAs?' (2018) 11 C.R. & I. 158-160.

concerns can be addressed through extending the pre-pack pool and the viability review to CVA cases.[112] Interviewee 8[113] is reinforcing this through the following statement:

> "I think that the pre-pack pool and the viability review are quite interesting and should apply to CVAs as well…People should be doing that anyway and I think that it is embarrassing it hasn't happened so."

If the pre-pack pool and viability review were available to CVAs, this could stimulate transparency and accountability when the sale is linked to connected parties. An impediment is that CVAs cannot stop secured creditors from enforcing their security and they must also provide their consent before the nominee proceeds with the court application.[114] This is conceivably an advantage in terms of insolvency finance since much of that finance comes from secured creditors. Secured creditors will give their consent to the CVA only if the rescue package affirms full returns. If secured creditors reject the CVA, it is expected that they will enforce their security against the company. This signifies that the survival prospects will be terminated and that the company will be liquidated.[115] The fact that a CVA binds only unsecured creditors and not secured creditors can be unfavourable since directors might hesitate to use CVAs because they would uncertain about its successfulness.[116]

Since IPs deal more often with administrations and liquidations, they have less experience in handling CVAs.[117] This preference is possibly linked with opportunistic

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[112] Ibid; Simon Clark, Gawain Moore, 'Calls for CVAs to be referred to the Pre-Pack Pool as concerns increase about their use' 19 June 2018 <https://www.walkermorris.co.uk/publications/calls-for-cvas-to-be-referred-to-the-pre-pack-pool-as-concerns-increase-about-their-use/> accessed 03 November 2019; see Chapter 4, Section 4.5.2. for the pre-pack pool.
[113] Interviewee 8 (Insolvency Practitioner) Big Four (London, UK, 19 January 2019); see Appendix D.
[114] Ibid 147.
[115] Ibid.
[116] IA 1986, s 4(3).
[117] Finch and Milman (n 39) 505.

reasons.[118] Administration post-EA 2002 has considerable costs, which includes high IPs fees[119] but IPs do not receive significant fees in CVAs. This could lead them in recommending administrations instead of CVAs, even in occasions where CVAs could be more advantageous.

Although CVA is considered more approachable in terms of costs, small companies still struggle to use it.[120] CVA is not merely described as costly but also time-consuming and have a certain level of complexity.[121] A company which is financially ailing will need to secure funding to be able to achieve a rescue. Companies need cash-flow for paying for the CVA costs and the continuation of trading. The deficiency of financing can cause a CVA termination, which can also be a general issue of most insolvency procedures.[122] A long-term finance arrangement for the company could be critical since if funding is not available, secured creditors would probably disagree with the CVA proposal. Moreover, suppliers might hesitate to continue trading with a CVA company without a finance back up.[123] Secured creditors can play a vital role to the economic survival of the company since if they finance the company they might be prioritised.[124] CVAs have flexibility and in many instances facilitate rescue funding but the broader flexibility of SoAs can address this problem more efficiently.[125]

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[118] John Flood et al., 'The Professional Restructuring of Corporate Rescue: Company Voluntary Arrangements and the London Approach' (ACCA Research Report 45, Certified Accountants Educational Trust, London, 1995).
[119] Elaine Kempson, 'Review of Insolvency Practitioners Fees: Report to the Insolvency Service' (July 2013) < https://www.gov.uk/government/publications/insolvency-practitioner-fees-a-review> accessed 4 October 2019.
[120] Walton, Umfreville and Jacobs (n 25) 12.
[121] Ben Larkin, Ben Jones, 'Company Voluntary Arrangements: an antidote to pre-packs?' Recovery (Summer 2009) 34.
[122] Walton, Umfreville and Jacobs (n 25) 58.
[123] Finch and Milman (n 39) 425, 429-430.
[124] Vanessa Finch, 'Corporate rescue: who is interested?' [2012] J.B.L. 190-212.
[125] For a comparison between CVAs and SoAs see Chapter 3, Section 3.6.

A successful rescue through a CVA is only possible when the mechanism is triggered before the company's financial state becomes terminal; with sufficient pre-organisation of the CVA; and with a healthy cooperation between the main company actors.[126] The lack of rescue finance is a fundamental factor that could cause the CVA to collapse therefore, if rescue finance encouragement devices are implemented, the position of CVAs could be enhanced.

A contemporary issue is that landlords feel disenfranchised with the CVA outcomes. The dilemma on whether landlords are oppressed bifurcated the courts in *BHS* and *Debenhams*.[127] The HM Revenue and Customs (HMRC) is usually the most committed creditor in a CVA and the one who will most likely vote against the proposal.[128] Arguably, if the HMRC supports CVAs, this tool could take a more rescue-oriented approach.[129] The return of the Crown[130] as a preferential creditor could be a drawback for CVAs given the lack of cram down on preferential creditors.[131] Before the abolition of the preferential status of the Crown in 2003, preferential creditors held the majority of assets.[132] In light of this upcoming change, the usage of CVAs might be disincentivised thus, alternatives – such as pre-packs – that could produce better stakeholder outcomes will be preferred.[133]

[126] Walton, Umfreville and Jacobs (n 25).
[127] See Chapter 3, Section 3.7.
[128] Walton, Umfreville and Jacobs (n 25) 3.
[129] Ibid 53-54.
[130] HM Treasury, Budget 2018 (HMSO, 2018), HC Paper No.1629; For a further discussion about the return of Crown preference see Chapter 2, Section 2.4.2.3.
[131] IA 1986, s 4.
[132] Andrew Keay, Peter Walton, 'Preferential debts: an empirical study' (1999) 3 Insolv. L. 112-118.
[133] Chris Umfreville, 'Pre-packaged administrations and company voluntary arrangements: the case for a holistic approach to reform' (2019) 30 I.C.C.L.R. 581-603.

3.6 Why is there a new lease of life for SoAs and not for CVAs?

Part 26 of CA 2006 now governs SoAs, that have been in operation since 1870[134] but have recently gained attention as a debt restructuring mechanism.[135] SoAs have multipurpose restructuring tools due to the flexibility that can be aligned to the financial necessities of the company.[136] SoAs can bind all creditors and members as long as the required voting majorities are satisfied and the judiciary grants an approval order. Although the court oversight transmits finality and certainty, SoAs can simultaneously be complex, time-consuming and expensive.[137] While SoAs are more expensive and cumbersome, they are still preferred to CVAs.

In the last few years, SoAs enjoyed renaissance and proved to be prevalent with foreign companies.[138] English courts approved forum shopping by allowing foreign customers to use SoAs. In *Re Algeco Scotsman PIK SA*[139] the decision was that forum shopping is allowed even if the purpose is just to use the United Kingdom (UK) SoA. A justification took effect through *Re Codere Finance (UK) Ltd*[140] in which good forum shopping took place. Snowden J in *Re Noble Group Ltd*[141] specified though that a sufficient connection with the English jurisdiction should be established. This is not a difficult task if financing operations that are potentially occurring in London are considered.[142]

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[134] Joint Stock Companies Act 1870.
[135] Payne, 'Debt Restructuring in the UK' (n 98).
[136] Louise Gullifer, Jennifer Payne, *Corporate Finance Law: Principles and Policy* (2nd edn, Hart Publishing 2015) 729.
[137] Ibid.
[138] Christian Pilkington, 'Schemes of Arrangement in Corporate Restructuring' (2014) 25 I.C.C.L.R. 366-367.
[139] [2017] EWHC 2236 (Ch).
[140] [2015] EWHC 3778 (Ch).
[141] [2019] BCC 349.
[142] David Milman, 'UK Restructuring Law: Recent Developments Considered' (2019) 418 Co L N 1-5.

SoAs are now used for takeovers, mergers, remodel and restructuring.[143] CVAs on the other hand are only available to companies with severe economic difficulties. Since SoAs can be used in several circumstances, they are not necessarily linked to insolvency. This means that directors who hesitate to use insolvency processes might be encouraged to use it before the company reaches a terminal stage.[144] CVAs are purely designed for distressed companies while SoAs can be utilised for purposes other than insolvency. This shows the SoAs's flexibility as well as the fact companies that are not financially troubled can use it.[145] The inclusion of SoAs in the 'Companies' Act and the inclusion of CVA in the 'Insolvency' Act further maintained this. This could also aid in keeping the value of the assets maximised and minimising the public outcry.

In CVAs, creditors and shareholders are not allowed to initiate a proposal, which is different to SoAs.[146] This flexibility gives the perception that the creditors are controlling the procedure. Without the cooperation of creditors, it will almost be impossible to take any procedure to the other end.[147] The court in the first hearing clarifies the composition of creditor classes as well as ensuring the adequacy of the provided information.[148] Creditors and members review the arrangement in their meetings and ultimately the SoA is subject to judicial sanction (second hearing).

CVAs are less expensive than SoAs mainly because CVAs are an out-of-court procedure thus, the court costs are avoided. As SoAs can be costly and accessible to mainly larger companies. As a result, small companies do not even take it into

[143] Van Zwieten (n 13) 575-576; Payne, 'Debt Restructuring in the UK' (n 98).
[144] Payne Ibid.
[145] Solvent restructurings through a SoA: *Re Telford Homes plc* [2019] EWHC 2944 (Ch); *In Re Charter Court Financial Services plc* [2019] EWHC 2680 (Ch); *Re Ophir Energy plc* [2019] EWHC 1278 (Ch).
[146] CA 2006, s 899(2).
[147] See further about this in Chapter 2, Section 2.4.2.1.
[148] CA 2006, s 896; Jennifer Payne, *Schemes of Arrangement: Theory, Structure and Operation* (CUP 2014) 2.2-2.3.

consideration.[149] If a SoA was available out-of-court, it could have been a cheaper and a less cumbersome procedure. However, an out-of-court procedure can lack accountability and transparency.

SoAs can be tailored in accordance to the interests of the creditors that provide the funding. Normally, existing secured creditors provide the funding – typically the company's main bank – who will only agree to furnish the finance if priority return is promised.[150] In SoAs, the creditor classes might be differentiated, for instance, by providing priority to creditors after the SoA instead of previous creditors, or separate senior creditors from junior creditors or secured creditors from unsecured creditors. David Richards J in *Re T & N Ltd*[151] stated that "… determining the correct classes of creditor, for which purpose the relevant criteria are the existing rights of creditors and their rights as affected by the scheme". Each class must undergo a separate meeting in which a majority of three-quarters of the present creditors or members must approve the SoA. Albeit this is a key issue, CVAs do not deal with creditor classes. This critical difference makes SoAs more appealing for companies. The separation of classes in SoAs might be fairer, but from the point of view of the company it might be more complicated. Cram down operates as an attention device for both SoAs and CVAs.[152] SoAs can cram down any creditor class but in CVAs only unsecured creditor votes can be overridden.[153] If in a CVA secured creditors or preferential creditors object to the proposal, the procedure will not go through. All secured creditors have to approve the CVA,[154] which could impact the level of CVA engagement.[155] If in a SoA a majority of

[149] Payne Ibid 215.
[150] Van Zwieten (n 13) 571.
[151] [2005] 2 BCLC 488.
[152] David Milman, 'Further judicial enlightenment on UK restructuring law and practice' (2014) 358 Co. L.N. 1-5.
[153] Ibid.
[154] IA 1986, s 4(3).
[155] McCormack and Yee Wan (n 21).

three-quarters is obtained at a creditor's meeting, it becomes binding to the remaining creditors (even if those creditors are secured or preferential).[156] Although minorities can be crammed down within a class in SoAs, the class that did not obtain the necessary votes will not be crammed down.[157] The SoA cram down device is more flexible than CVA but not as broad as Chapter 11.[158] The ICG Report 2018 considered introducing a cross-class cram down device analogous to Chapter 11, in which some respondents supported that the 'absolute priority rule' (APR) included in Chapter 11 should also be considered.[159] This rule provides that senior creditors should be paid before a junior creditor, but an exception applies when the senior creditors consents to that payment. The government highlighted their concern about allowing this rule since they are of the opinion that it will obstruct flexibility. Also, although this is not within the purposes of this thesis, since USA is taken as an exemplary the ARP abuse incidents should be studied. The government is now considering a version of APR that would provide flexibility and at the same time minimise the risk of abuse.[160]

3.7 Do CVAs operate as an unfair tool for landlords?

Since CVA schemes can have a flexible scope, future liabilities can be taken into consideration.[161] This kind of liabilities include rents, which means that several landlords can be affected.[162] In retail and high street restaurant CVAs, trade creditors

[156] CA 2006, s 899(1).
[157] Sarah Paterson, 'Reflections on English Law Schemes of Arrangement in Distress and Proposals for Reform' (2018) 15 European Company and Financial Law Review 472.
[158] See Chapter 6, Section 6.2.2.2 for Chapter 11 in the USA.
[159] Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) 5.156-5.168 (ICG Report 2018).
[160] Ibid 5.164-5.168.
[161] *Doorbar v. Alltime Securities Ltd* [1995] BCC 1149; *Re Cancol Ltd* [1995] BCC 1133; *Re Sweatfield Ltd* [1997] BCC 744; *Beverley.*
[162] Julie Gattegno, 'What does the Debenhams decision mean for retail CVAs?' (2019) 1940 E.G. 107-109.

are not impacted, while the landlords are somewhat compromised[163] with terms that go beyond the CVA duration. Arguably, the attraction towards CVAs by retail companies occurs due to the cunning mechanism that was identified by retailers to reduce rents. They tried to justify their position through arguing that a more constructive restructuring can be pursued. The British Property Federation supports that since CVAs are improperly utilised, this will ultimately harm the reputation of the UK insolvency regime thus, they are calling on the government to review CVAs.[164] The above discussion is linked with the interviewees' 1 and 7 excerpts below respectively:

> "I am in favour of CVA in the sense that they give creditors a vote and involvement and I do think that they need to be changed somehow so that they are not used as a way of reducing rent overheads."[165]

> "Companies are basically trying to pick out particular types of creditors and treat them unfairly. Landlords are the classic example of that, but I think that the courts are good in a way that they are making sure that does not happen. I think that the real problem in CVA is the fact that the company directors try to find creditors who are of less worth than other creditors in order to treat them differently and they always pick landlords. I think that all creditors should be treated equally

[163] Oliver Shah, 'Department store giant's CVA plan faces backflash' The Sunday Times, 27 May 2018, 1.
[164] British Property Federation, 'British Property Federation calls government for urgent review of CVAs', 7 June 2018, <https://www.bpf.org.uk/media-listing/press-releases/british-property-federation-calls-government-urgent-review-cvas> accessed 02 November 2019; B Barrison, R Varma, 'CVAs: blame the game or the player?' (2018) 1829 E.G. 54-55.
[165] Interviewee 1 (Credit Manager) (By phone, UK, 04 December 2018); see Appendix D.

and it is actually wrong to treat some creditors better than others."[166]

When these interviewees were asked whether they believe that CVAs are an oppressive mechanism for landlords, they maintained a different opinion and perception. Landlords believe that CVAs are used in an abusive manner since future rents are reduced and lease terms are re-written. According to landlords, all other creditors are fully repaid, which is happening at their expense.[167] Shah stated that: "Landlords have long been ambivalent about CVAs. That ambivalence is turning into outright hostility."[168] CVAs are widely regarded by the landlord community as unfair since they are likely the only affected class of creditors as their opinion cannot usually alter the CVA outcome. Landlords also believe that CVA decisions could include provisions that do not necessarily influence company rescue since CVAs seem to affect rents post-CVA. Furthermore, they maintain that retailers are alleviating property liabilities without dealing with fundamental problems that are practically damaging the company to the core. Frankly, rent levels have never been associated with the financial instability of companies therefore, by not identifying the underlying issues that deteriorate the company, the CVA will not be successful for the company. Retailers support that they are overcharged since high street rents reach a high amount that is not compatible with the current economic climate of the UK high street.[169] That said, this opinion indicates that CVAs aid in bringing justice to the current situation and not for abusing the features that are provided by the procedure.

[166] Interviewee 7 (Lawyer/Academic) a law firm and a UK university (London, UK, 15 January 2019); see Appendix D.
[167] Shah (n 163).
[168] Ibid.
[169] Felicity Toube, 'CVAs - landlords lose out' (2019) 32 Insolv. Int. 157-159.

In *BHS*, the retailers targeted to reduce rents during a CVA. In this case, the company entered a CVA after the landlords agreed to a rent compromise. The CVA was twinned with administration but the company continued to struggle. The company then exited the CVA but a dispute between the landlords and the liquidators emerged. Landlords argued that according to clause 25.9 of the CVA they were entitled to receive the difference of the compromised rent post-CVA termination. They also said that rents should be included in the insolvency expenses. The liquidator argued that clause 25.9 is not an enforceable penalty clause and that it would be against the *pari passu* rule to pay some unsecured creditors in priority of others. The courts clarified that the normal contract law principles do not directly apply on CVAs thus, permission was granted for the landlords to get the whole sum of the compromised rents. The judge also held that the *pari passu* rule was not breached as CVA was of temporary nature that did not intend to continue disadvantaging landlords after termination. This was arguably a victory for the landlords but *Debenhams* comes to dispute this.

Debenhams is a major case to come into court during the recent retail climate, which was brought into court for grounds of unfair prejudice and material irregularity. A CVA can be challenged on the grounds of unfair prejudice or material irregularity even though it is difficult to prove.[170] *Debenhams* tried to address the disputes between landlords and retailers hence, it would be essential to evaluate the decision. In this CVA approximately 95 per cent of all creditors voted in favour and 82 per cent of landlords agreed with it. Landlords who are severely impacted by the CVA terms cannot usually influence its outcome. In this case the contractual rent and property were categorised in accordance with the store's performance. The rent was altered to be paid monthly instead of quarterly and the landlord's right to forfeit was precluded. There was a

[170] IA 1986, s 6(1); see Chapter 3, Section 3.3.3.

provision about reviewing the rent either after the lease expiry or the end of the CVA period, which means that the rent of some stores might remain unchanged. The first ground, that the applicant landlords brought into court, was that landlords cannot be categorised as creditors for future liabilities who fall within IA 1986, s 1. The court's decision on this ground was that the definition of debt has a broad meaning in the sense that it can include future rent since they are pecuniary contingent liabilities. In the second ground, the landlords argued that a CVA cannot function in a way that it would ease the reduction of future rents since it is automatically linked to unfair prejudice. The landlords were given the option of either terminating the lease or agreeing to reduced rents thus, the courts held that the rent can be subject to change by a CVA and that this is not necessarily unfair since CVAs did not enforce any new obligations but just altered the current ones.

While in the past it was stated that landlords still have the right of forfeiture unless it is stated by the CVA,[171] now the High Court in *Debenhams* has clarified that the right to forfeit is a proprietary right that cannot be varied by the CVA. The courts divulged that this is an aspect of the CVA that just needs to be severed therefore, the CVA will not be discarded. Landlords also argued that their auspiciousness in comparison to other unsecured creditors was restricted without justification. Landlords said that the objective justification can only be legitimate in circumstances where a differential treatment could lead to company rescue, which was not the situation in this case. This was about business reality where international suppliers would not be expected to understand CVAs. Hence, the judge held that due to the long-term contract with the landlords, which was beyond market rates compared with the short-term

[171] Anna Jeffrey, 'Company voluntary arrangements: landlord issues and remedies' (2018) 11 C.R. & I. 60-61.

suppliers – that were paid in accordance with the market rates – it was justified that this was necessary for the company to have a prospect of survival. The court added that this would have been unfair if the reduction of rents went below the market rates. This clarification is practically giving scope for further challenges that relate to valuation.

The judge in *Debenhams* dealt only with situations that arose in the particular case but there are various issues regarding CVAs that could be challenged, and it still remains questionable as to which aspects are indeed unfair. In other words, this case has encountered several issues that concerned landlords for a while but there are conceivably issues that have not been answered yet. The landlords will presumably appeal the decision and there will probably be further litigation that will deal with balancing the interests of struggling retailers and landlords. Since this is an area that is currently experiencing a gradual evolution, it is expected that the judiciary will have to balance the further disputes in the future.[172] Arguably, in the last few years CVAs were vigorously pushing the boundaries, since before *Debenhams,* the landlords were on a certain extent idle. This emboldened the retailers to carry on exploiting the circumstances but now the purpose of the challenge is to attain an improved treatment for landlords. Although this might be overoptimistic, the ideal would be to see some statutory changes on CVAs that would address the imbalance and elucidate a fairer outcome for all creditors.[173]

[172] Supported by James Morgan QC in *Williams v. Carraway Guildford (Nominee A) Ltd* mentioned above.
[173] Umfreville, 'Pre-packaged administrations and company voluntary arrangements' (n 133).

3.8 Conclusion: Should CVAs be abolished or streamlined?

The CVA mechanism is encountering several economic, social and moral problems.[174] CVAs before the IA 2000 were in privacy, which comes in contrast to the CVA with a moratorium and administration.[175] Even though a moratorium has positive consequences to the company by protecting it from the creditors, it also carries with it publicity which could harm future trading and the goodwill of the company. The addition of a moratorium but with some alterations to other procedures, in theory might be ideal, but in practice it will produce more costs and complications. The leading rescue procedure is still the streamlined administration, which overshadows CVAs and any other rescue procedure.[176] Even if CVAs are streamlined will they manage to become one of the core procedures in corporate insolvency? After evaluating various aspects of the procedure, the answer is arguably no.

Milman and Akintola in their response to the Insolvency Service Service's consultation on the corporate insolvency framework stated that: "What should be done in our view is that the rescue framework within our insolvency regime should be streamlined in such a way as to get rid of inefficient procedures, such as CVAs".[177] Sometimes the intention of CVA usage is not purely for targeting rescue, yet Umfreville, Walton and Jacobs suggest that CVA is a flexible process that should remain within the legislation.[178] They have also highlighted that although several companies can benefit from it, success can sometimes be ambiguous because external factors can impact this.

[174] Hiestand and Pilkington (n 84).
[175] Keay and Walton, *Insolvency Law* (n 22) 147.
[176] See Chapter 4 for an analysis about administration.
[177] The Insolvency Service, A Review of the Corporate Insolvency Framework response form (25 May 2016).
[178] Walton, Umfreville and Jacobs (n 25).

Chapter 4 – Administration

4.1 Introduction

The Cork Committee pointed out three vital points regarding corporate rescue: that the potential rescue of the company should be undertaken in timely a fashion to have a better prospect of success, the company should be entitled to a period in which it should be protected from hostile acts by creditors or other parties, and that the interests of all stakeholders should be taken into account.[1] In light of the aforementioned, the Committee ultimately created administration, which was introduced as the main rescue procedure through the Insolvency Act 1986 (IA 1986).[2] This chapter has the aim of evaluating the effectiveness of administration, with the empirical aspect of this research amplifying the accountability of the recommendations that are about to follow. Conjectures as to the impact of the exit of the United Kingdom (UK) from the European Union (Brexit) on administration in the UK are highlighted, as the fate of the process at a European level is indistinct.

A cornerstone of the UK insolvency regime was the Enterprise Act 2002 (EA 2002) amendments to the IA 1986, which *inter alia* included the streamlined administration. This new style administration is radically different from the original version in terms of initiation and execution. According to the statistics, administration prior to the EA 2002 was not well utilised.[3] In 2003, the number of administrations remained below 1000 but the numbers in the following years started to gradually

[1] Report of the Review Committee on Insolvency Law and Practice (Cmnd 8558, 1982) (Cork Report); Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 302.
[2] Andrew Campbell, 'Company rescue: the legal response to the potential rescue of insolvent companies' (1994) 5 I.C.C.L.R. 16-24.
[3] The Insolvency Service Statistics (Company Insolvency Statistics: October to December 2019), <https://www.gov.uk/government/statistics/company-insolvency-statistics-april-to-june-2019> accessed 19 February 2020.

increase. In 2008, 4822 administrators were appointed, which was the highest number that has ever been recorded.[4] Even though the number of administrations has reduced since 2014 (below 2000 administrations per annum), it is still more approachable than the old-style administration. Interestingly, there is an apparent increase from 2018 to 2019 from 1462 to 1814 administration appointments respectively.

Low insolvency statistics do not necessarily signify a stability in the economy. More pejoratively, the statistics are potentially suggesting that zombie companies exist or that informal rescue procedures have gained more attention or that administration is inaccessible for several companies due to the high expenses.[5] The Insolvency Rules (IR 2016) that were brought into force in April 2017 could help in this regard. The aim of the fee estimates that were introduced by IR 2016, r 18.16(4) was to address the criticisms on the transparency of the office-holder fees.[6] Provisions regarding cost saving were also introduced by IR 2016, Pt 1, Ch.9. Specifically, the 2016 rules specified that physical meetings are not necessary and the creditors are given the option of opting out from receiving documents, notices and information from office-holders.[7] Every jurisdiction that aims to have an effective rescue mechanism should develop methods that provide easier access to rescue finance.[8]

One of the reasons that the streamlined administration procedure was introduced was because it was conceived that administrative receivership (AR) was not a suitable choice for distressed companies.[9] Secured creditors had more trust in AR, which

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[4] Ibid.
[5] David Milman, 'The treatment of the corporate insolvency regimes under the Insolvency (England and Wales) Rules 2016: a navigator's guide' (2017) 393 Co. L.N. 1-4; Finch and Milman, *Corporate insolvency law* (n 1) 324.
[6] Kayode Akintola, 'The prescribed part for unsecured creditors: a pithy review' (2017) 30 Insolv. Int. 57.
[7] Ibid 58.
[8] See Chapter 4, Section 4.7.
[9] DTI/Insolvency Service White Paper, *Productivity and Enterprise 'Insolvency – A Second Chance* (Cm 5234, 2001)

resulted in the underuse of administration. The EA 2002 practically substituted AR with the new administrative procedure.[10] The access to the old administration was problematic and lacked thought such as on issues concerning exit from administration.[11] The out-of-court administrator appointment[12] and the specification of the hierarchy of objects of administration were the main changes that were included in the reform. Undoubtedly, the availability of administration without a court order created propitious consequences since the length, the complexity and the cost of the procedure were alleviated.[13] This is not always the case though since an out-of-court appointment of the administration could be challenged at the court based on the validity of the underlying charge.[14] This chapter also targets to reveal the adequacies and limitations of the streamlined administration. Within the arguments that follow is the fact that the streamlined administration is often disguised AR.[15]

A critical aspect that motivates companies to use administration is the moratorium. The moratorium is a shield that protects the company from parties that may seek to take legal or enforcement action against it during administration.[16] Recent cases reinforce the view that the moratorium could be exploited by the company directors.[17]

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[10] The Insolvency Service, 'Enterprise Act 2002 – Corporate Insolvency Provisions: Evaluation Report' January 2008 <http://webarchive.nationalarchives.gov.uk/20080610162953/http://www.insolvency.gov.uk/insolvencyprofessionandlegislation/legislation/EA02CorporateInsolvencyReport.pdf> accessed 06 October 2019; EA 2002, s 250.

[11] Gill Todd, 'Administration Post-Enterprise Act – What Are the Options for Exits?' (2006) 19 Insolv. Int. 17-20.

[12] Vanessa Finch, 'Re-invigorating corporate rescue' [2003] J.B.L. 527-557; IA 1986, Sch B1, para 14.

[13] Ibid.

[14] *SAW (SW) 2010 Ltd v. Wilson* [2018] Ch 213 (CA).

[15] See Chapter 4, Section 4.2.1, 4.2.3 and Chapter 5, Section 5.6; For a deeper analysis of this argument see Kayode Akintola, David Milman, 'The rise, fall and potential for a rebirth of receivership in UK corporate law' (2019) Journal of Corporate Law Studies <https://www.tandfonline.com/doi/full/10.1080/14735970.2019.1631551> accessed 29 September 2019.

[16] The occasions in which the moratorium is lifted are examined in Chapter 4, Section 4.4.1.

[17] *Re Cornercare Ltd* [2010] EWHC 893 (Ch); *JCAM Commercial Real Estate Property XV Ltd v. Davis Haulage Ltd* [2017] EWCA Civ 267.

Therefore, cases that are potentially mirroring actions of misuse require a thorough analysis that could lead to the mitigation of this position.[18]

An unintended result of the 2002 reform was the vast growth of pre-packaged administrations (pre-packs) in mid-2005.[19] This chapter maintains that the emergence of pre-packs post-EA 2002 was due to the similarity of pre-packs with AR in terms of rescue outcomes.[20] The trading of the company during a rescue procedure is important, thus financing the company is vital for continuance of the entity. A pre-pack agreement could ensure that the company will receive the desirable funding. This pre-arrangement provoked great attention after 2002 but the number of pre-packs have started to drop.[21] According to the Graham Review, pre-packs still attract massive criticism, which is disproportionate to the figures.[22] This chapter discovers the rationale behind bad reputation of pre-packs, their effect and impact towards stakeholders.

4.2 The three hierarchical objects of administration and the impact on creditors

The EA 2002 came into force on 15 September 2003, which included the three objects of administration. The hierarchical order for the objects is to save the company as a going concern;[23] to achieve a better result for creditors than in liquidation;[24] and realise the property for preferential and secured creditors.[25] The first two objects are on the

[18] See Chapter 4, Section 4.4.2.
[19] Sandra Frisby, 'A preliminary analysis of pre-packaged administrations' (R3: Association of Business Recovery Professionals, 2007); See an analysis about pre-packs in Chapter 4, Section 4.5.
[20] See Chapter 4, Section 4.5.3
[21] Pre-Pack Pool - annual report 2018, (May 2019) <https://www.prepackpool.co.uk/uploads/files/documents/Pre-Pack-Pool-2018-Annual-report-v4.pdf> accessed 07 October 2019.
[22] Graham Review into Pre-pack Administration, Report to the Rt Hon Vince Cable MP, June 2014. <https://www.gov.uk/government/publications/graham-review-into-pre-pack-administration> 27 September 2019.
[23] IA 1986, Sch B1, para 3(1)(a) (objective A).
[24] IA 1986, Sch B1, para 3(1)(b) (objective B).
[25] IA 1986, Sch B1, para 3(1)(c) (objective C).

level of rescuing the company and/or its business, whereas the third and last option prevails to the abandonment of rescue in any sort of way.[26] The third option is what would have happened in AR where there is not enough realisation for the general body of creditors. The moratorium aids administration, which protects the company against legal proceedings from creditors during administration.[27] There was a discussion about these objectives in a previous chapter,[28] but what follows is an extensive evaluation of the objectives and suggestions on advancing their competence. The results of the statistical analysis – that were conducted for the purposes of this thesis – reinforce the discussions about administration.

4.2.1 Rescue the company as a going concern

The primary legislative purpose of administration is to save the company as a going concern. The company remains intact and the business continues – or a portion of it – as a going concern.[29] Saving a company as a going concern has a different result and meaning than rescuing the business as a going concern.[30] Harman J in *Re Rowbotham Baxter Ltd*[31] stated that the survival of the company is an option only if the whole or part of the corporation is considered as a going concern. This objective is what diverges the streamlined administration with AR. The AR value lies within the fact that it facilitates asset realisation whereas a company rescue strategy can take place in an

[26] Harry Rajak, *Company Rescue and Liquidation* (3rd edn, Sweet & Maxwell 2013) 92.
[27] IA 1986, Sch B1, para 42-44; Ian Fletcher, 'UK Corporate Rescue: Recent Developments — Changes to Administrative Receiverships, Administration Company Voluntary Arrangements — The Insolvency Act 2000, The White Paper 2001 and the Enterprise Act 2002' (2004) 5 E.B.O.R. 119.
[28] See Chapter 2, Section 2.4.1.
[29] Andrew Keay, Peter Walton, *Insolvency Law: Corporate and Personal* (4th edn, Jordan Publishing 2017) 82.
[30] See the discussion in Chapter 2, Section 2.4.
[31] [1990] BBC 113.

administration.[32] However, the pursuance of rescue and/or trading of the company is not necessarily within the spectrum of AR.[33] The prime purpose of administration is rarely used or envisaged, since it is difficult to be obtained in practice. The statistical results of the database of the author of this thesis is confirming this. Objective A is the least favoured since only 17 out of 600 companies pursued this objective and solely 3 out of those companies managed to actually save the company or part of it.[34] Indeed, the company rescue is a target that is almost never achieved[35] partly due to reputational damage to the goodwill of a company in insolvency. Another reason is that there are challenges with breaking up non-viable parts of a company and that new owners might desire a new business vehicle. Ultimately the pursuit of this objective is – or at least it should be – an economic decision. Katz and Mumford estimated that less than 10 per cent of administrators attempt to accomplish this object[36] since it is contemplated as the most challenging one.

The promotion of company rescue through the EA 2002 was of secondary importance as a collective approach towards creditors was more essential.[37] Yet, the relevant statistics signify that the low uptake of this objective does not justify its existence. That said, if the Parliament insists to retain this objective, solutions must be proposed that could possibly limit its failure. As previously mentioned in this section, the reputational damage of the company is a drawback that restricts the promotion of this objective. The directors' late intervention when the company is in distress obstructs the productive usage of this objective. This effectively comes into conflict with the

[32] For further see Chapter 4, Section 4.2.3; Akintola and Milman (n 15).
[33] *Ahmad v. Bank of Scotland* [2016] EWCA Civ 602.
[34] Further empirical results on all the objectives can be found in Chapter 2, Section 2.4.2.
[35] Keay and Walton (n 29) 83.
[36] Alan Katz, Michael Mumford, 'Study of administration cases' (2007) 20 Insolv. Int. 97-103.
[37] Rebecca Parry, 'United Kingdom: Administrative Receiverships and Administrations' in Katarzyna Gromek Broc, Rebecca Parry (ed.), *Corporate rescue: An overview of recent developments from selected countries* (Kluwer Law International 2006)157.

legislator's intention of initiating this objective with the aim of encouraging directors to aid the ailing company at a preliminary stage.[38] This is possibly happening due to the negative perception of "insolvency", which admittedly Parliament has tried to address.[39]

4.2.2 Achieve a better result for the company's creditors than in liquidation

If the initial purpose of administration is not attainable, then the next available object is to protect the interests of the creditors by ensuring a better return for them than in liquidation. Most administrators target the second aim of the legislation since 378 out of 600 companies chose this objective.[40] This happens because it is less controversial than the third one and more approachable than the first one when the company is in grave economic debt. The administrator is required to perform his duties by weighing the interests of the company creditors. *Re Logitext UK Ltd*[41] highlights that an administration can have a better result for the creditors than winding up. During administration the company must be a going concern, thus the economic value of the assets can be maximised.[42] If the rehabilitation of the entity is not a viable scenario, secured and preferential creditors are prioritised in terms of returns. Thus, an analysis about the returns that they receive through administration is material. The House of Lords suggested that even though company rescue is the first objective: "We do not want an administrator to have to pursue a company rescue that would be reasonably practicable but would result in a lower return to creditors…"[43]

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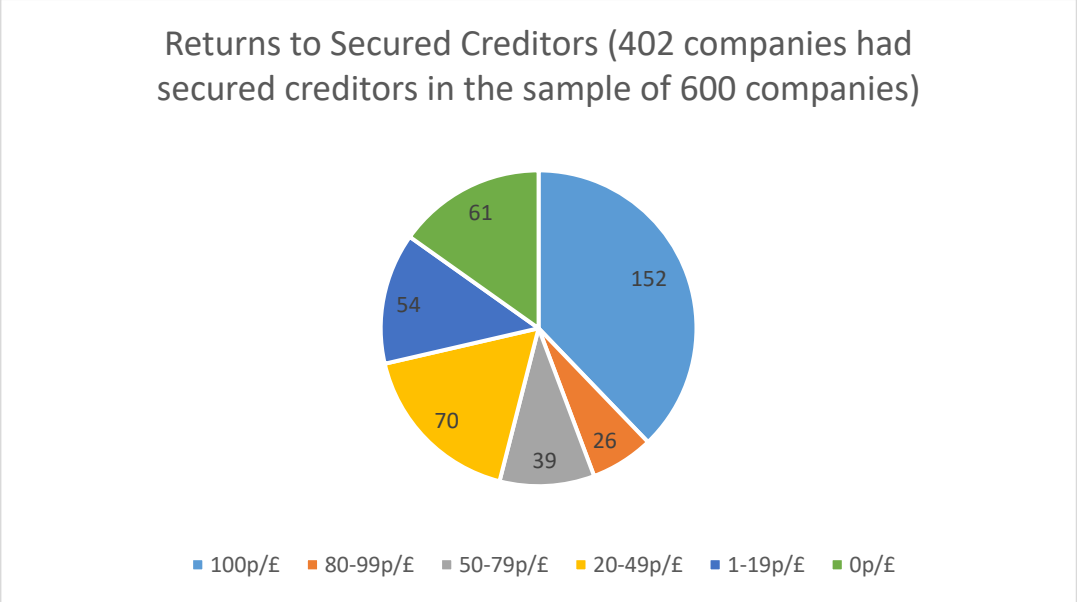
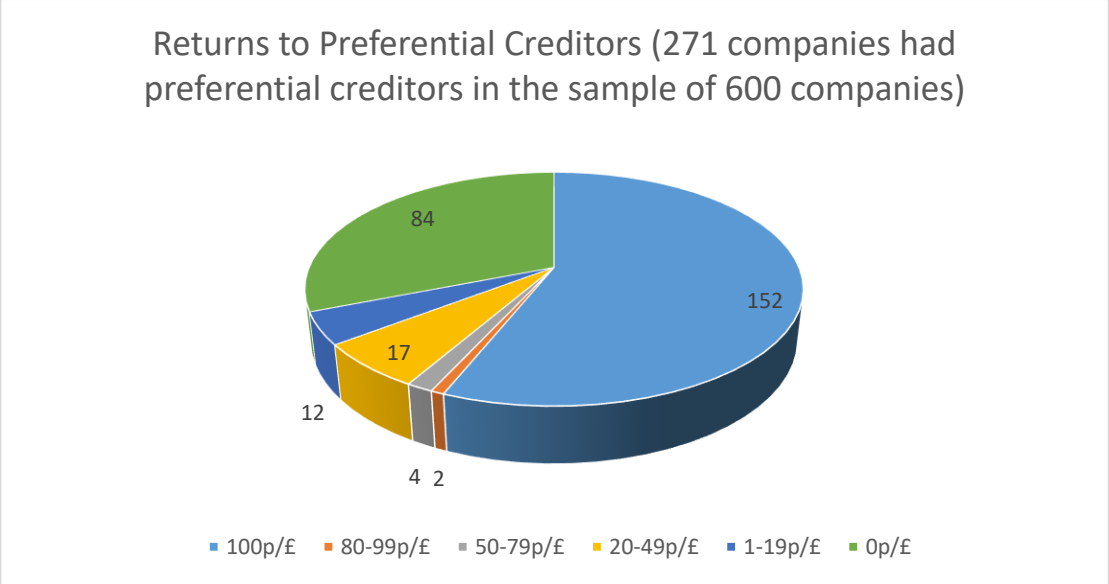
[38] Mark Phillips, Jeremy Goldring, 'Rescue and reconstruction' (2002) 15 Insolv. Int. 75-78; John Armour, Audrey Hsu, Adrian Walters, 'The Impact of the Enterprise Act 2002 on Realisations and Costs in Corporate Rescue Proceedings' (December 2006) Insolvency Service Report, 22.
[39] John Tribe, 'The Rhetoric of Insolvency Law' (2009) SSRN <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1329112> accessed 07 December 2019.
[40] See Chapter 2, Section 2.4.2, Graph B.
[41] [2005] 1 BCLC 326
[42] Katz and Mumford (n 36).
[43] Hansard, House of Lords, Vol 639, 21 Oct 2002 col. 1100 and 1102.



Graph A[44]

An illustration of the returns that creditors received in the sample of 600 companies of the database is important for pinpointing the administration effectiveness. Graph A above shows that the secured creditors of 152 out of 402 companies received 100p in the £, constituting 38 per cent of total secured creditors in the sample. 26 and 39 of those 402 companies received 80-99p in the £ and 50-79p in the £ respectively. The 15.17 per cent of secured creditors of this sample received 0p in the £, while 13.4 per cent of creditors received 1-19p in the £.

[44] In accordance with the database of the author of this thesis.

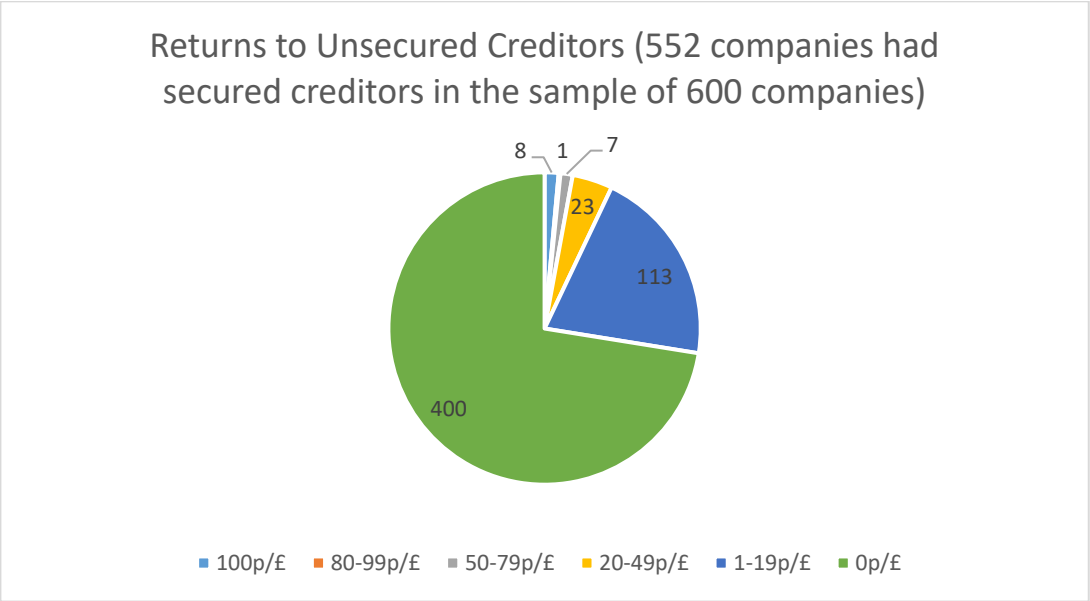


Graph B[45]

Administration envisages the collective interests of creditors therefore, this section investigates the returns to preferential and unsecured creditors. Graph B shows that preferential creditors of 152 out of a sample of 271 companies received 100p in the £, which reaches the 55.9 per cent of all preferential creditors of the database. Preferential creditors of 6 companies received 50-99p in the £ while 29 preferential creditors received 1-49p in the £. Yet, preferential creditors of 84 companies that represent the 31.1 per cent of all preferential creditors of the sample got 0p in the £. While administration can be successful at a certain level for secured and preferential creditors – as a substantial number of secured/preferential creditors were fully repaid – most unsecured creditors are disadvantaged. This happens because unsecured creditors rank low in the waterfall,[46] which means that normally there is not anything left for them.

[45] In accordance with the database of the author of this thesis.
[46] *Re Lehman Brothers International (Europe) (In Administration)* [2017] UKSC 38 (*Lehman case*).

Although it has been argued that unsecured creditors are in a better position than pre-EA 2002 due to the prescribed part,[47] it seems that they are still exposed.



Graph C[48]

Graph C results about unsecured creditors are evidential to the above arguments. This is justified by the fact that unsecured creditors of 400 of 552 companies had a 0p return in the £, which represents the 72.5 per cent of the total unsecured creditors in the sample. The 20.5 per cent of the unsecured creditors of the sample received 1-19p in the £, while unsecured creditors of 31 out of 552 companies got 20-99p in the £. Unsecured creditors of 8 out of 552 companies were auspicious enough to receive full returns.

Funding administrations is a crucial problem[49] since the first and the second object usually have voluminous costs. Objective C also requires funding to operate but to a lesser extent. The challenge here is to appraise whether there are enough assets that would ease a deal with a fixed charge creditor or a factoring firm. By overriding the

[47] See more in Chapter 2, Section 2.4.2.3.
[48] In accordance with the database of the author of this thesis.
[49] See Chapter 4, Section 4.7.

cost barrier, it could engender benefits for all stakeholders. In other words, funding will be available that would facilitate the pursuance of value maximising strategies. Financing the company is vital to all creditors because the administrator's expenses and fees are top-sliced from corporate assets covered by a floating charge. The administrator's breadth of powers extent to selling the profitable parts of the business, which generates immediate cash flow.

In contrast to the first objective, the second objective allows the realisation of the company assets without trading administration. The moratorium and the breadth of powers of the administrator which include the distribution to certain creditors,[50] to deal with charged and owed property, strengthen sale and trading.[51] Hence, these powers are theoretically capable of saving time and costs as well as achieving the UK insolvency framework's ideal of collectivity.[52]

4.2.3 Realise the property of the company to distribute it to the company secured or preferential creditors

The third option can only be applied if the previous two options are exhausted. The administrator must ensure that the interests of creditors are protected as a whole. If the viability of the company and the business sale are no longer obtainable, the assets must be sold for the benefit of secured and preferential creditors.

[50] IA 1986, Sch B1, para 65, 66.
[51] IA 1986, Sch B1, para 71, 72; Sofia Ellina, 'Administration and CVA in corporate insolvency law: pursuing the optimum outcome' (2019) 30 I.C.C.L.R. 180-191, 185.
[52] *Re Agrokor DD* [2017] EWHC 2791 (Ch); *Re Stanford* [2010] EWCA Civ 137; Sandra Frisby, 'In Search of a Rescue Regime: The Enterprise Act 2002' (2004) 67 M.L.R. 247-272, 249; Kristin Van Zwieten, *Goode on Principles of Corporate Insolvency Law* (5th edn, Sweet & Maxwell 2019) 7; John Armour, Sandra Frisby, 'Rethinking Receivership' (2001) 21 O.J.L.S. 73-102

The administrator must act promptly, effectively and operate in a way that protects the interests of the creditors.[53] As per the IA 1986, Sch B1, para 74, the administrator's mission can be relatively onerous because the creditors may bring an action for misfeasance against him/her. The action could occur on grounds of unfair and harmful decisions, or because s/he did not act as quickly and sufficiently as s/he should have done.[54] The Court of Appeal in *Coyne v. DRC Distribution Ltd*[55] stated that if administration takes a wrong turn from the beginning it would be difficult for the company to recover. Meanwhile the courts are wary of interfering with the work of administrators because the administrator's administrative and commercial decisions are not issues that the courts ordinarily handle.[56]

The statistical analysis about the objectives of administration manifest that one out of three administrators carry out the functions of this purpose.[57] The sale of assets though is the prevalent outcome of administration.[58] The third purpose arguably provides a 'compensation' for the abolition of AR.[59] A similar feature of these two procedures is that the administrator and the receiver take the control of the company in their hands. In both procedures, the directors have no authority over the company. The company might continue employing the directors though, since their contracts might not be terminated. Therefore, if contracts of docile directors are adopted, these would be treated as expenses, paid in priority to the fees of the administrator. The particular director who undertakes valuable work for the company is not fairly treated since s/he

[53] *Re Atlantic Computer Systems plc* [1992] All ER 476.
[54] David Milman, 'Administration: an evolving regime for distressed companies' (2014) 351 Co. L.N. 1-5.
[55] [2008] BCC 612.
[56] *Re T & D Industries plc* [2000] 1 BCLC 471; *Re CE King Ltd* [2000] 2 BCLC 297; see Chapter 3, Section 3.3.3 and 3.7 for unfairness in a CVA; For a further discussion about the commercial judgment of the courts see Chapter 5, Section 5.5.2.
[57] See Chapter 2, Section 2.4.2, Graph B.
[58] 388 out of 600 companies had an asset sale as their outcome; See more in Chapter 2, Section 2.4.2, Graph C.
[59] Ian Corfield, 'Administrations: do they work and for whom?' (2013) 24 T.P.A. & A. 85-87.

ranks at the bottom of the expenses ladder. The apparent resemblance of objective C and AR indicates that AR never departed with the effect of the EA 2002.[60] Administration is a disguised AR since the actual result of objective C can be identical.[61] This is reinforced by scholars such as McCormack who describe administration "as 'receivership-plus' and as 'receivership with a few add-ons'" and Willcock who argued that " … the new deal is merely 'son of receivership'".[62] Moreover it has been characterised as "'transmutation' or 'merger' of the administrative receivership and administration procedures".[63] In the light of the fact that objective A pursuance is infrequent, in reality administration and AR are used for ensuring debt recovery to the qualifying floating charge holder (QFCH).[64] Another mutual component that is strengthening this view is that QFCHs can request the administrator's and administrative receiver's appointment.[65]

Why not place the company under liquidation immediately instead of having a third option? The rationale behind the third option is that it is another political concession to secured creditors for the abolition of AR. That said, there is an economic logic to it if the administrator is seen as a trustee or custodian of corporate assets. A company should only access administration if it is a going concern, which indicates that the value of assets will certainly be noticeably higher than in liquidation.[66] Therefore,

[60] Gerard McCormack, 'Control and Corporate Rescue - An Anglo-American Evaluation' (2007) 56 I.C.L.Q. 515-551, 535-536; Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (EE Publishing 2008) 55.
[61] Kayode Akintola, Sofia Ellina, 'The Use and Abuse of Corporate Insolvency Rescue Procedures: A Contextual Evaluation of the United Kingdom and Cyprus' in Jennifer L. L. Gant (ed.), *Party Autonomy and Third-Party Protection in Insolvency Law* (INSOL Europe 2019) ISBN 978-0-9931897-7-7, 137-154.
[62] McCormack, 'Control and Corporate Rescue - An Anglo-American' (n 60); John Willcock, 'How the Banks Won the Battle for the Enterprise Bill' Recovery (June 2002) 24-26.
[63] Stephen Davies (ed.), *Insolvency and the Enterprise Act 2002* (Jordans 2003) 40.
[64] Akintola and Milman (n 15).
[65] See Chapter 4, Section 4.3 for a further discussion about the appointment of the administrator.
[66] Look Ho, Rizwaan Mokal, 'Interplay of CVA, administration and liquidation: Part I' (2004) 25 Comp. Law. 3-8.

in some occasions it is in the best interests of the creditors to undergo an administration instead of liquidation.[67] Interviewee 8,[68] noted that:

> " Administration is an easier to get into process so sometimes that is the reason why companies go into administration rather than liquidation…administration is certainly perceived by the public and by the business community to be at least a rescue of the business and if not always a rescue of all of the business or all of the jobs at least it has connotations about rescuing the business, liquidation does not and as a result if a company goes into administration it tends I think to provide some support for keeping the asset value higher than it would be in liquidation. I think that once the company goes into liquidation then everyone thinks that the assets are going to be sold at a very low valuation whereas in administration there is the opportunity for some other value to be maintained."

This interviewee emphasises that administration can sometimes function as disguised liquidation.[69] According to the database of this thesis, secured creditors of only 70 out of 245 companies that ended up in an asset realisation were fully repaid while the 20.8 per cent of those creditors received 0 pence in the £. This percentage is not uncommon since through using administration – instead of liquidation – companies can hide behind their financial difficulties. The same interviewee also included the following thought:

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[67] *Oakley-Smith v. Greenberg* [2002] EWCA Civ 1217.
[68] Interviewee 8 (Insolvency Practitioner) Big Four (London, UK, 19 January 2019); see Appendix D.
[69] For the link between administration and liquidation see: Andrew Keay, 'The future for liquidation in light of the Enterprise Act reforms?' [2005] J.B.L. 143-158; David Milman, *Governance of Distressed Firms* (EE Publishing 2013) 18; CVAs can also be used as disguised liquidations.

> "There is a perception that administration is not the end of the business and therefore people may pay higher prices for assets and there may be a connotation that the business is continuing and therefore at least some of the goodwill or continuity is being maintained. I don't think you get that in liquidation and therefore it makes in my mind the third objective an acceptable one in terms of you know the reason for administration."

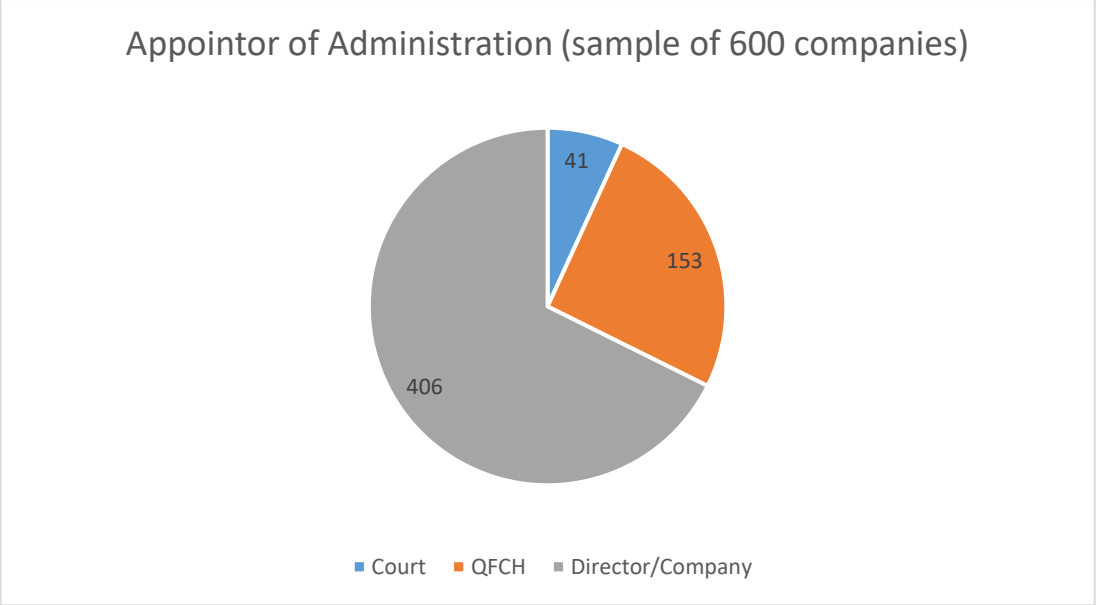
This interviewee provides a reasoning for the disguised liquidations through suggesting that administration can also be utilised by companies that want to keep their value maximised. He further highlights that this happens to create the perception that the company is not entirely deteriorated and that with a viable restructuring plan the company could overcome distress. Therefore, if the enterprise manages to survive, to some extent the goodwill of the company can possibly be kept sustained. However, this strategy should be discouraged as this could supress the rights of unsecured creditors who could have lower probabilities of receiving anything.[70] Graph C above, is evidence of the onus that unsecured creditors are encountering as a result of administration. Simultaneously, only one out of the 205 companies that pursued objective C gave full returns to unsecured creditors, while 47 and 38 companies fully repaid their secured creditors and preferential creditors respectively. This is justified by the fact that objective C does not consider unsecured creditors at all[71] as the straightforward aim is to pay secured/preferential creditors. The exposure of unsecured creditors after administrations is vast yet, the secured and preferential creditors returns can be salutary.

[70] Sandra Frisby, 'Interim Report to the Insolvency Service on Returns to Creditors from Pre- and Post-Enterprise Act Insolvency Procedures' (July 2007) 38.
[71] IA 1986, Sch B1, para 3(2)(4).

4.3 Initiation of Administration

An administrator can be appointed by the court;[72] or by the company/director;[73] or by QFCH. [74] These initiation methods helped administration to become more approachable by companies since it reduced costs and simplified the procedure. Insolvency Practitioners (IPs) must keep in mind that if the procedure is not followed properly the administrator's appointment is invalid. An out-of-court appointment can be challenged through the court. An example is *Saw* in which the nature of the administrator's appointment was challenged on the basis that the QFCH was in breach of the negative pledge that was in favour of the secured creditor. Another key ground was the issue of lightweight floating charge[75] but this was justified through *Re Croftbell Ltd*[76] where the usage of lightweight floating charges was approved. Even though there were various disputes, the court held that the appointment of the administrator by the QFCH was valid.[77]

[72] IA 1986, Sch B1, para 10.
[73] IA 1986, Sch B1, para 22.
[74] IA 1986, Sch B1, para 14.
[75] A charge obtained for the sole aim of appointing an office-holder.
[76] [1990] BCLC 844.
[77] See a further analysis of the case in Gabriel Moss, 'Lightweight, featherweight and phantom floating charges *SAW (SW) 2010 Ltd v Wilson'* [2018] Ch 213 (CA)' (2018) 31 Insolv. Int. 125.



Graph D[78]

Pre-EA 2002, an administrator could only be appointed through a court order. This option is still available post-EA 2002 and is used in potentially contentious administrations such as foreign companies that move their centre of main interests (COMI) to the UK. This method of appointment is a residue of the old administration. An obstacle of the old administration was that it was a court driven, which means that it was inaccessible in comparison to other procedures due to the expenses and the cumbersome process. Graph D above shows that only 41 out of 600 administrators (2012-2016) were appointed through a court order. This is signifying that the concerns about the court driven administration were legitimate. The application can be made by the company, the directors, any of the creditors or the designed officer of the magistrates' court.[79] The application can also be initiated by the company liquidator,[80] the CVA supervisor[81] and the Financial Conduct Authority.[82] Appointments through the

[78] In accordance with the database of the author of this thesis.
[79] IA 1986, Sch B1, para 12.
[80] IA 1986, Sch B1, para 38.
[81] IA 1986, Sch B1, para 12(5), s 7(4)(b).
[82] Financial Services and Markets Act 2000, s 359.

court are usually used by to unsecured creditors when there is not a QFCH.[83] The court might reject an administrator's appointment, when there could have been a solution through arbitration for creditor claims.[84] The court should consider the best interests of creditors on deciding whether to grant the administrator's appointment.[85] However, the final decision of whether to authorise the administration order is within the court's discretion. When the court believes that the statutory requirements have been satisfied, the court may decide to issue the order anyhow even if most creditors are against it.[86]

In practice, most administrations are initiated by the company/director out-of-court. Graph D confirms this as it indicates that 406 administrators were appointed by the company/director. The company/directors are entitled to appoint an administrator only if the company is not already in administration or liquidation. After the company's difficult economic position is verified, the secured creditors encourage the company to appoint an administrator who has to be approved by them.[87]

The company/directors must submit a notice to the court about the administrator's appointment.[88] If a QFCH is involved s/he must be notified about the intention of appointment five business days in advance.[89] In *Re Minmar (929) Ltd v. Khalastchi*[90] the administrator's appointment was not followed properly. Thus, flexibility was given by the Deregulation Act 2015 through some technical alterations. According to the Deregulation Act 2015, s 19 and Sch 6, para 5, an administrator can be appointed while a liquidation petition is extant. IA 1986, Sch B1, para 25A, specifies

[83] David Milman, 'Administration under Sch.B1 to the Insolvency Act 1986: recent developments' (2017) 394 Co. L.N. 1-5.
[84] *Fieldfisher LLP v. Pennyfeathers Ltd* [2016] EWHC 566 (Ch).
[85] Keay and Walton (n 29) 81.
[86] IA 1986, Sch B1, para 55; *Re Maxwell Comminications Corp plc* [1992] BCLC 465; *Re Structures & Computers Ltd* [1998] 2 BCLC 292.
[87] Kayode Akintola, 'What is left of the floating charge? An empirical outlook' (2015) 7 JIBFL 404.
[88] IA 1986, Sch B1, para 27.
[89] IA 1986, Sch B1, para 26.
[90] [2011] BCC 485.

that an administrator can be appointed as long as the notice of intention to appoint an administrator (NOI) was provided before the petition for liquidation was presented. It appears that through the above changes the risk of abusing administration to obstruct winding up is limited. The interim moratorium takes place immediately after the NOI is filed to the court.

Following *Minmar* other cases challenged administrator's appointments. The intention to ease administration through introducing e-filing might have been legitimate, but the challenges generated unexpected problems. Several cases encountered problems with e-filing appointments in 2019.[91] It seems that the problem still continues in 2020 with *Re Carter Moore Solicitors Ltd*.[92] A central issue that is resurfacing in these cases is the inconsistency between Practice Direction Insolvency Proceedings para 8 and Electronic Practice Direction para 2.1. Since the court's opinion is occasionally inconsistent a further confusion is established. The judiciary in *Woodside v. Keyworker Homes (North West Ltd)*[93] tried to avoid the depreciation of these rules through intelligibly explicating them. These challenges arguably make the introduction of out-of-court administration futile. Judge Cooke in *Causer v. All Star Leisure*[94] conveyed that the mere existence of these challenges indicate that the answers are equivocal therefore, controversial provisions need to be recontextualised to verify concomitance that would avoid these challenges when inattentive actions take place. The voluminous cases on e-filing led to a provisional Practice Guide from the High Court's Chancellor Sir Geoffrey Vos on 29 January 2020. He specified that it is up to

[91] *Re NJM Clothing Ltd* [2018] BCC 875; *Re Towcester Racecourse Ltd* [2019] BCC 274; *Re Spaces London Bridge Ltd* [2019] BCC 280; *Wright v. HMV Ecommerce* [2019] EWHC 903 (Ch); *Edwards v. SJ Henderson & Co Ltd* [2019] EWHC 2742 (Ch); *Re Skeggs Beef Ltd* [2019] EWHC 2607; *Causer v. All Star Leisure* [2019] EWHC 3231 (Ch).
[92] [2020] EWHC 186 (Ch).
[93] [2019] EWHC 3499 (Ch).
[94] [2019] EWHC 3231 (Ch).

the court who is dealing with the subject matter case to determine the validity of that e-filing appointment. However, he also highlights that this is expected to be addressed through revising the IR 2016.

After 15 September 2003, the QFCH's ability to appoint an administrative receiver was abolished although it is subject to exceptions.[95] The reform compensated QFCHs through providing the option of appointing an administrator out-of-court. The QFCH should give two days' notice to any former QFCH[96] and a notice of appointment must be submitted to the court.[97] The results of Graph D above are consistent with the qualitative data analysis that Akintola conducted where approximately the 78.4 per cent of administrators were appointed by the company/directors, the 19.3 per cent of appointments were by QFCHs and the 2.3 per cent by the court.[98] These results manifest that QFCHs do not exploit the opportunity of initiating administration out-of-court that was provided to them post-EA 2002. This does not mean that secured creditors did not comprehend that administration can function as a method of maximising their returns. Indeed, it seems that this is not the case since Akintola – after taking a closer investigation on the appointments that were made by company/directors – he suggested that QFCHs are usually keen in persuading the company/director to appoint an administrator.[99] In situations where the company/director initiated administration, QFCHs approved the prospective administrator. Secured creditors are circumspectly choosing the cases where they will act as appointors. The purpose is to abstain from

[95] EA 2002, s 250; IA 1986, s 72A-H; Frisby, 'Interim Report to the Insolvency Service' (n 70).
[96] IA 1986, Sch B1, para 15(1)(a).
[97] IA 1986, Sch B1, para 18.
[98] Akintola, 'What is left of the floating charge?' (n 87).
[99] Ibid.

reputational risk, but this tactic is static since the insolvency outcome in due course is contiguous.[100]

4.4 The Moratorium

The moratorium is an unvarying feature of administration since 1986 and a notable aspect of administration.[101] While the company is in administration, the status quo of the company regarding its assets is preserved. The moratorium forbids any enforcement proceedings by creditors or any other party against the company.[102] For instance, QFCHs are usually threatened when a company is having trouble on repaying its landlords. The consequence is that it will be impossible for the company to be sold if landlords proceed with repossession. The moratorium may positively aid the company to maintain intact and simultaneously attempt to save the company during that certain period.[103] When the moratorium is in force the company can pursue value maximisation. Various strategies, such as ensuring the preservation of company customers and receiving the maximum value that can be attained by the service or goods to the customer occur.[104]

The moratorium duration is subject to the followed administration route. If the appointment of an administrator is through the court, the moratorium takes place when the application is made. When administration is initiated – by QFCHs or directors – the moratorium is triggered once the NOI is filed.[105] The director's notice lasts for ten

[100] Ibid.
[101] David Milman, 'Moratoria in UK insolvency law: policy and practical implications' (2012) 317 Co. L.N. 1-4.
[102] *Re Atlantic*.
[103] Keay and Walton (n 29) 98.
[104] Brian Rawlings, 'Trading in administration: a manufacturer's tale' Recovery (Summer 2010) 25.
[105] For the interim moratorium see IA 1986, Sch B1, para 44.

business days and the QFCH's notice lasts for five business days.[106] The company has an extended moratorium when the company officially enters administration.[107]

Creditors should be mindful that their security rights are not eradicated[108] but delayed from being enforced. Nevertheless, the moratorium does not restrict the creditor from implementing a contractual right where s/he is explicitly authorised to do so, in case of a financial distress. Commonly, the moratorium does not restrain the creditor from executing contractual rights as regards to debts between the company and the creditor unless they constitute steps taken to enforce security.[109]

The administration moratorium persuades companies to use administration because it provides them the advantage of a "breathing space".[110] Directors and administrators might have viewed this feature as way of obtaining extra time that allows them to avoid any creditor proceedings. *JCAM* shed some light on this issue.[111] The possibility of further loss is an adequate concern for creditors since the longer the company remains in a moratorium the danger increases.[112] The impact on unsecured creditors can be even more severe. However, this is an instance where a minority has to suffer for the wider good, which one could describe as a form of utilitarianism.[113] With a lengthy moratorium, there will probably be nothing left for unsecured creditors though as they rank last in terms of distribution.[114] Notwithstanding, if the company manages

[106] Ibid.
[107] IA 1986, Sch B1, paras 42-43.
[108] *Re Niagara Mechanical Services International Ltd* [2000] 2 BCLC 425; David Milman, 'The administration moratorium: a fresh twist to the tale' (2003) 2 Insolv. L. 60; David Milman, 'Moratoria on enforcement rights: revisiting corporate rescue' (2004) Conv. 89-108.
[109] Geoffrey Yeowart, 'UK restructuring moratorium: a useful option for company rescue?' (2010) 11 JIBFL 657.
[110] Finch and Milman, *Corporate insolvency law* (n 1) 302.
[111] For a further analysis see Chapter 4, Section 4.4.2.
[112] G Pont, L Griggs, 'A Principled Justification for Business Rescue Laws: A Comparative Perspective (Part II)' (1996) 5 IIR 47.
[113] Ellina (n 51).
[114] *Lehman.*

to achieve a turnaround the creditors would benefit from the whole procedure. A moratorium could be easily mistreated in terms of use; therefore, the moratorium should be carefully designed in terms of cost, entrance and extent.

4.4.1 What are the Boundaries of the Moratorium?

If the moratorium is breached, actionable damages will be available depending on the substance of the violation.[115] With the administrator's or the court's approval, the moratorium can be lifted. If the administrator is not convinced that that there is a valid reason for lifting the moratorium, the opinion of the court can be sought.[116] The courts will consider whether the advantages of the person who requires to proceed with possession are balanced with the benefits of other creditors.[117] The question that troubled the courts in *Unite the Union, McCarthy & Others v. Nortel Networks UK Limited (in administration)*[118] was whether the employees could claim their owed money by lifting the moratorium during administration.[119]

In *Nortel,* the employees' claims fell into the following five sections: protective award; unfair dismissal; breach of contract; expenses claims; and discrimination claims. The administrator granted his approval to the employees to proceed with the protective award but not with the other four sections.[120] The *AES Barry v. TXU Europe Energy*[121] case reflects the fact that each case is treated uniquely as the court is depending on the

[115] *Euro Commercial Leasing Ltd v. Cartwright & Lewis* [1995] 2 BCLC 618.
[116] IA 1986, Sch B1, para 43(2); *Re Atlantic.*
[117] *Innovate Logistics Ltd v. Sunberry Properties Ltd* [2009] BCC 164 CA.
[118] [2010] EWHC 826
[119] A similar concern was addressed in *Hudson & Others v. The Gambling Commission (Re Frankice (Golders Green) Limited)* [2010] EWHC 1299 (Ch).
[120] Radford Goodman, 'Testing the boundaries of the administration moratorium' (2011) 4 C.R. & I. 51-52.
[121] [2004] EWHC 1757 (Ch).

severity of the circumstances.[122] In *Safe Business Solutions Ltd v. Cohen*[123] the moratorium lift was granted since most of the administration goals were fulfilled. Consequently, the moratorium can be lifted in situations where the court is convinced that there has been a breach from the company or when administration is at a final stage, or where the grant of leave to enforce is unlikely to conflict with the administration object.[124]

4.4.2 Is the moratorium an abusive tool?

There is an apparent trend of using administration for the sole purpose of taking advantage of the moratorium. The courts have been more than willing to take a wider view on hostile activities that fall within the scope of the moratorium.[125] For example, the directors may choose to enter an administration with a strategy, via submitting various notices with the aim of obtaining a longer moratorium for the company.[126] In *Re Cornercare Ltd* the judge stated that " … an unscrupulous individual or group of individuals could engineer a continuing moratorium by filing repeated notices of intention to appoint, each giving rise to an interim moratorium. If that did happen I have no doubt that the court would have adequate power to treat that as an abuse and act accordingly."[127] Another case that was concerned with whether the moratorium was invalidly accessed was *Re Business Dream Ltd*[128] because it was thought that the intention of filing the NOI was to avoid a creditor's voluntary liquidation. The

[122] Goodman (n 1).
[123] [2017] EWHC 145 (Ch).
[124] *Re Atlantic* second ground.
[125] *Carr v. British International Helicopters Ltd* [1994] 2 BCLC 474; *Re Axis Genetics plc* [2000] BCC 943; Milman, 'The administration moratorium' (n 108).
[126] Chris Umfreville, 'A review of the corporate insolvency framework: a new moratorium to help business rescue?' (2016) 385 Co. L.N. 1-4.
[127] [2010] EWHC 893 (Ch).
[128] [2011] EWHC 2860 (Ch).

conclusion of these two cases was that the duration of NOI is ten business days but there is no restriction on filing a subsequent notice. Therefore, the extension of the moratorium was not obstructed. The aforementioned cases raised the issue of underhanded behaviour by certain individuals, yet problems were not addressed to the core. They just stated that if there is evidence that directors improperly used the administration moratorium the NOI will be ineffective.

Directors occasionally file the NOI for strategical reasons without having the aim of saving the company. The Insolvency Intelligence stated that: "It seems that it has been common practice to file notices of intention with no such settled intention simply in order to protect the company with an interim moratorium."[129] Since these actions give rise to ethical issues, Umfreville suggested that there should be a guidance for IPs, which is signifying that the Insolvency Code of Ethics should be subject to revision.[130]

JCAM scrutinised and reinforced the above points. In this case, Davis Haulage Limited (DHL) company was facing economic distress during 2015. DHL was threatened that the landlord will proceed with possession and that the HM Revenue and Customs will proceed with the liquidation of DHL. The director – with the purpose of avoiding both threats – decided to file a NOI hence, a moratorium was created for ten business days since the administrator was not appointed. Three consecutive NOIs that expressly stated the need of the moratorium were filed right after the previous one expired. This means that this method allowed a 56-day moratorium. DHL's director submitted a CVA proposal and the next day he filed a fourth NOI. The action of the director purely demonstrates that his purpose was to safeguard the moratorium's

[129] Insolvency Intelligence 'Filing a notice of intention to appoint an administrator' (2017) 30 Insolv. Int. 59.
[130] Chris Umfreville, 'Curtailing the use of multiple notices of intention to appoint administrators: the case for a moratorium?' (2017) 395 Co. L.N. 3.

extension.[131] The appellant was seeking an order that would vacate and remove the fourth NOI on abusive grounds. The director stated that the uncertainty of getting the CVA approved is what led him to administration. The director justified this through saying that the risk of not getting an approval for a CVA with a moratorium was high, since DHL might not have been eligible because the company was not considered as a small company. The issue that the Court of Appeal dealt with was whether the director should have had the intention to actually enter administration. David Richards LJ denied blaming the individual director or his advisors for their actions, but he specified that the continuous NOI filings was an abuse of the insolvency procedure. The judiciary concluded that the improper use of the notice should cease. The Court of Appeal held that the order for the NOI removal should be issued since it was wrongfully given in the first place. With the acceptance of the fourth notice, directors would have been encouraged to invalidly exploit the moratorium.

If a conciliatory process was available, it could facilitate the cooperation between directors and landlords via the administrator. The conciliatory procedure is a common insolvency procedure in France that enables the parties to come to a consensual agreement.[132] Before *Jervis v. Pillar Denton Ltd (Re Game Station)*[133] companies entered administration with the sole aim of avoiding to pay a large rent amount which left the landlords exposed.[134] However, since *Re Game Station,* the ranking of rents and rates for premises used in administration are no longer in doubt.[135] This case clarified

[131] Jonathan Lopian, 'What are your intentions? The interim administration moratorium and *JCAM Commercial Real Estate Property XV Ltd v Davis Haulage Ltd*' (2017) 10 C.R. & I. 96-98.
[132] Paul Omar, 'Four models for rescue: convergence or divergence in European insolvency laws? Part 2' (2007) 18 I.C.C.L.R. 171-180.
[133] [2014] EWCA Civ 180.
[134] Sally Lynch, 'Game on: tackling the impact of Game -- a look at the Clinton Cards liquidation' (2016) 9 C.R. & I. 137-140.
[135] Anne Sharp, Katharina Crinson, Margaret Rhodes, 'Game over: rent as an administration expense on a pay as you go basis' (2014) 7 C.R. & I. 57-59.

that rents during administration are now being considered as an administration expense.[136] The availability of funding is vital since it would facilitate the usage of the premises.

When interviewee 8[137] was asked whether he thinks that the administration moratorium is abused, he replied that:

> "I would agree the interim moratorium period is a confusing period but it can be used as a period for preparation for sale. The one thing that often happens in that period is that directors don't know who to pay, they are concerned over their personal position … and I think your question was whether it was abused and I think that it has been abused. I think there should be a clear limit of how long that period should be because the longer it goes on, the more difficult it becomes."

According to the interviewee's views, directors are practically taking advantage of the interim moratorium for planning purposes, but this does not mean that the process is not improperly utilised. The moratorium's misuse creates further negative consequences to the company that should keep the directors alert. When a NOI is submitted for indecent reasons, procedural hearings follow that aim to determine whether there was indeed an abuse. The court's involvement could influence the reduction of corporate value and assets if the company eventually goes into administration. The hearing expenses would be a burden to the economically ailing company since these costs are extractable from corporate assets.

[136] Finch and Milman, *Corporate insolvency law* (n 1) 345.
[137] Interviewee 8 (n 68).

Some of the recommendations expressed that eligibility criteria of a CVA with a moratorium should be revised or add a preliminary moratorium to the legislation.[138] Another solution could be to extend the ten business days period to the moratorium after the first filing of the NOI. The additional days would give sufficient time for the director to take valuable decisions on whether administration is the appropriate procedure for the circumstances.

4.4.3 Is a preliminary moratorium needed?

A moratorium is merely allowed in two situations: by initiating an administration or a CVA. As there are several criteria for using CVA with a moratorium, the majority of companies might not be eligible.[139] The promotion of a preliminary moratorium has been recommended in recent and past consultations but this still remains as an idea.[140] One recommendation was to make CVA with a moratorium available to larger companies instead of including an independent moratorium process.[141] The 2019 directive on preventive restructuring frameworks, indicates that the member states of the European Union (EU) should include a moratorium/stay in their legislation and it specifies that the moratorium should not go beyond four months.[142] Although after Brexit the UK might not be bound to this, the UK legislators will certainly be influenced by the EU insolvency changes. The main intention for legislating a pre-insolvency

[138] The Insolvency Service, Proposals for a Restructuring Moratorium - a consultation, (July 2010).
[139] Discussed in Chapter 3, Section 3.4.
[140] Insolvency Service July 2010 (n 138); The Insolvency Service, A Review of the Corporate Insolvency Framework: A consultation on options for reform the Corporate Insolvency Framework response form (25 May 2016)(2016 Consultation); Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) (ICG 2018 Report).
[141] Ibid 2016 Consultation; Umfreville, 'Curtailing the use of multiple notices of intention to appoint administrators' (n 130).
[142] Directive (EU) 2019/1023 (the 2019 directive), Article 6; For a discussion about the 2019 directive's proposals see Nicolaes Tollenaar, 'The European Commission's proposal for a Directive on preventive restructuring proceedings' (2017) 30 Insolv. Int. 65-81.

moratorium is to provide time to companies that would allow them to reconsider their options regarding rescue.[143] One should evaluate though whether the moratorium as a gateway procedure would restrict the indecent approach towards the administration moratorium.

A plausible concern about the moratorium as a standalone procedure is that the weaknesses might predominate the advantages. The opinion of experts about the preliminary moratorium is divided, and this is accentuated by the following interviewee excerpts:

> "I think that the directors have got to make a decision. Either they are comfortable and they can pay their creditors in full or they are not. If they are not, they should get out of the way and let somebody else take over the business of the company. I think that it is absolutely wrong to allow a standalone moratorium."[144]

> "I see that as a positive move and that it gives people the opportunity to discuss the situation going forward than agreed behind closed doors.[145]"

> "It is a very different proposal on a very different proposition because if that becomes legislation it will show very clearly what the directors can and cannot do in that period, who is responsible for what, what the waterfall is if things don't go well…I think that it would be a useful tool generally in

[143] ICG report (n 140) 42–59.
[144] Interviewee 7 (Lawyer/Academic) a law firm and a UK university (London, UK, 15 January 2019); see Appendix D.
[145] Interviewee 1 (Credit Manager) (By phone, UK, 04 December 2018); see Appendix D.

> insolvency to have a director's moratorium, if I can call it that, and have a 5-day notice of intention to appoint an administrator. I think the latter is confusing in almost every case, but it gives time for that final negotiation on the sale of the business, if that is needed."[146]

R3 and interviewee 8 above agree that a preliminary moratorium will be a useful tool for insolvent companies[147] since it will provide time for negotiations and restructuring plans. R3 also stated that the preliminary moratorium "[c]ould lead to more comprehensive, and sustainable, rescue plans or restructurings than are currently feasible".[148] Companies that use CVAs, often combine them with administrations for the moratorium thus, the availability of a moratorium as a standalone procedure could makes things less complicated for these companies.[149] However, through examining this from another angle it "seems wishful thinking rather than a clear benefit".[150]

Interviewee 7 in the above excerpt indicates that the initiation of a preliminary moratorium could take an undesirable direction. The introduction of a new form of protection for the company, could result in opening Pandora's box since the directors might roguery exploit the new procedure. Theoretically though, the availability of the independent moratorium to insolvent companies could confine the intentional improper usage of the administration interim moratorium. The inclusion of restrictions to the pre-insolvency moratorium is an essential element of avoiding other more serious repercussions. If for instance the directors manipulate the preliminary moratorium by

[146] Interviewee 8 (n 68).
[147] R3 Response, A Review of The Corporate Insolvency Framework (July 2016).
[148] Ibid.
[149] Lorraine Conway, 'Company Voluntary Arrangements (CVAs)' (31 May 2018) House of Commons Briefing Paper, Number 6944, 5.
[150] Umfreville, 'A review of the corporate insolvency framework' (n 126).

temporarily avoiding liquidation, this will have as a consequence the business/asset value deterioration.[151] Therefore, this can diminish the availability of dividends.

The 2018 consultation suggests that the moratorium should be available to companies that are not already insolvent but to companies that will become insolvent if intervention does not occur.[152] This could be a flaw for this tool there is a certain complexity in determining the vicinity of insolvency. The tests used for determining this are the balance sheet test and the cash-flow test.[153] When the company is not yet on the verge of insolvency but there are some difficulties, the director will probably consider alternative means of recovery, by continuing trading instead of draining the remaining available funds of the company with the usage of a preliminary moratorium.[154]

The UK insolvency regime lacks a single process that combines a moratorium and a cram down. A common strategy to achieve this is through twinning administration with schemes of arrangement (SoAs). Payne suggests that this is not an ideal solution though since this combination can be time-consuming, expensive, impact taxation and the creditors could add constraints that could cause predicaments to the company.[155] She further supports that a moratorium as a standalone procedure could minimise any strenuous consequences. The moratorium is a main reason for a lot of companies to use administration hence, this might mean that if an independent moratorium is introduced, administrations will be reduced. The reality is that various queries endure as to which is the most suitable way of encountering this issue.[156] A preliminary moratorium seems

[151] Jennifer Payne, 'The role of the court in debt restructuring' (2018) 77 Cambridge Law Journal 124-150.
[152] ICG 2018 Report (n 140) 5.26-5.29.
[153] *BNY Corporate Trustee Services Ltd v. Eurosail-UK 2007-3BL Plc* [2013] UKSC 28.
[154] Marc Brown, 'The evolution of the Enterprise Act 2002?' (2019) 32 Insolv. Int. 122-125.
[155] Jennifer Payne, 'Debt Restructuring in the UK' (2018) 15 European Company and Financial Law Review 449-471, 465.
[156] Umfreville, 'A review of the corporate insolvency framework' (n 126).

complicated and expensive thus, not suitable for smaller companies since they would not be able to bear the high costs.[157] After *JCAM* the issue became more controversial since it resulted in resurfacing the debate on whether there should be a moratorium as a gateway procedure. Hence, the development of this area is imminent and one of the aims should be to eliminate potential abuses.

The preliminary moratorium duration should be carefully observed since if the moratorium's length is too flexible, the interests of the creditor could be jeopardised by the actions of the directors or by other external factors.[158] A small or medium-sized enterprise (SME) that is already facing financial turmoil, might not be capable of bearing the costs. If the SME does not secure funding, a three-month moratorium could only be approachable to large companies. R3 reinforces the view that the extension of the pre-insolvency moratorium could lead to complexities, costs, and value drainage.[159] If the extension of the moratorium is ambiguous and vague, the reputation of the UK Insolvency regime could be gravely harmed. However, if a preliminary moratorium takes place and fails to achieve a workout, the company might then go into administration. If an administration moratorium is triggered though, it could be inequitable and contrary to the tenets of contract law to hold proprietary rights in abeyance in this way. A solution to this could be to abolish the administration moratorium.

The preliminary moratorium is a measure of amplifying the sense of rescue culture in the UK since it provides an alternative to companies that do not bear a strict

[157] Company Law Newsletter 'Insolvency Service consults on proposal for a moratorium for companies restructuring their debts' (2010) 279 Co. L.N. 1-4.
[158] Chris Umfreville 'Mora' the same: reflecting on the latest attempts to salvage company rescue' (2017) 28 I.C.C.L.R. 385-392.
[159] R3 Response (n 147).

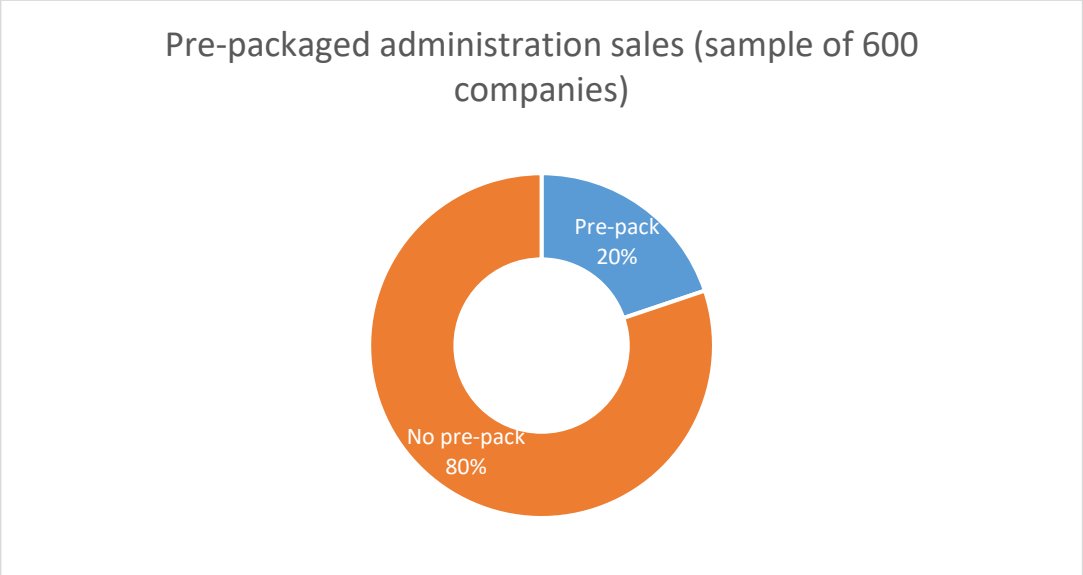
insolvency concept.[160] Brown suggests that: "the tightly restricted entry criteria and the practical difficulty with their application, together with the necessary costs in respect of the monitor to protect the interests of creditors, means that the use of such a moratorium is likely to be very limited."[161] For the pre-insolvency moratorium to work, its aims and parameters should be established openly. The CVA with a moratorium is a cumbersome procedure[162] therefore, by changing the current procedure, the odds reveal that its attractiveness will not increase. Cynically speaking there is not an ideal procedure but there could be an amelioration of some procedures in a manner of reaching an optimum stage. It might be more advantageous to improve the administration moratorium rather than adding more complicated and costly procedures to the insolvency law.[163]

4.5 Pre-packaged administrations (Pre-packs)

Pre-packaged sales were previously used for ARs, [164] but after the EA 2002 the emergence of pre-packs was bolstered due to the allowance of out-of-court administrations.[165] Since 2005 there were many insolvency debates on the controversial issue of pre-pack administrations.[166] The government, the media, commentators, the judiciary and creditors have periodically exerted criticism towards pre-packs.[167] The pre-pack pool statistics logged that 30.7 per cent of all administrations in 2018 were

[160] Brown (n 154).
[161] Ibid.
[162] See Chapter 3, Section 3.4.
[163] The Insolvency Service, A Review of the Corporate Insolvency Framework response form (25 May 2016).
[164] Marcus Haywood, 'Pre-pack administrations' (2010) 23 Insolv. Int. 19.
[165] Peter Walton, 'Government consultation: is it time to re-pack the pre-pack?' (2010) 273 Co. L.N. 1-4.
[166] Frisby, 'A preliminary analysis of pre-packaged administrations' (n 19).
[167] Vanessa Finch, 'Pre-packaged administrations and the construction of propriety' (2011) 11 JCLS 1-31; Kate Creighton-Selvay, 'Pre-packed administrations: an empirical social rights analysis' (2013) 42 ILJ 85-121.

pre-packs,[168] while as it can be seen in Graph E below, that 20 per cent of those administrations were pre-packs. This shows that there is an interest towards the path of pre-packs, but several doubts and problems are generated. However, pre-packs can be beneficial therefore, an investigation of their effect is valuable for the deductions in this thesis.



Graph E[169]

A pre-pack is a prior arrangement in which a new company must buy the old business. The business marketing is little or non-existent and this arrangement is implemented once administration starts. [170] The intention here is not necessarily to form a proposal that would save the company but an arrangement that secures the sale of the viable

[168] Pre-Pack Pool - annual report 2018 (n 21).
[169] From the quantitative database that was formed by the author of this thesis.
[170] Statement of Insolvency Practice 16 - Pre-Packaged Sales in Administrations (January 2009), <https://www.r3.org.uk/media/documents/technical_library/SIPS/SIP%2016%20E&W.pdf> 06 October 2019.

business of the company. The courts or creditors do not have to approve pre-packs thus, an administrator is permitted to undertake a pre-pack deal without prior consent. [171]

Before conducting pre-packs, IPs must ensure that the company's turnaround was infeasible.[172] The administrator is responsible for determining whether the company's failure is evident and detect whether the quick business/asset sale through a pre-pack is an efficient solution. Subsequently, the business somehow survives but is not intact. Pre-packs seem to be in the best interests of the creditors since they receive more debt returns than in liquidation.[173] Arguably, pre-packs facilitate the second objective of administrations since pre-packs aim to produce efficiency towards the interests of creditors.[174] Funding that could aid the company to continue trading might not be available hence, some companies would benefit if they undergo a pre-pack sale before entering administration. Current and potential creditors might be reluctant to provide a further amount of money to the dying company.[175] Even though pre-packs have been censured, there are some justifications for their existence. For example, enterprises with intellectual property and goodwill prefer to pursue pre-pack deals since the asset value could drop vigorously after entering an insolvency procedure.[176]

Although pre-packs are almost invisible to the legislation,[177] this process is acknowledged by the judiciary.[178] A regulating mechanism of pre-packs is available through the Statement of Insolvency Practice (SIP 16), which was revised and came

[171] *Re Transbus International Ltd* [2004] 1 WLR 2654.
[172] Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (EE Publishing 2016) 72.
[173] Finch, 'Pre-packaged administrations' (n 167).
[174] Xie, '*Comparative Insolvency Law*' (n 172) 79.
[175] Keay and Walton (n 29) 119.
[176] Geoff Meeks, J Gay Meeks, 'A Gouldian View of Corporate Failure in the Process of Economic Natural Selection', Centre for Business Research, University of Cambridge (2002).
[177] Stephen Davies, 'Pre-pack—He who pays the piper calls the tune' Recovery (Summer 2006) 16.
[178] *DKLL Solicitors v. HMRC* [2007] BCC 908; *Re Johnson and Machine Tool Co Ltd* [2010] BCC 382; *Re Hellas Telecommunications (Luxembourg) II SCA* [2009] EWHC 3199 (Ch).

into effect on 1 November 2015. SIP 16 is frequently revised with the attempt of harmonising the actions of IPs.[179] All IPs are obliged to follow the rules of the SIP 16 that monitor all parameters that concern pre-packs. SIP 16 signifies an effort of mitigating issues of transparency through the disclosure of the IP's purposes before s/he is appointed as an administrator.[180] Per SIP 16, administrators are required to report the majority of their actions to the creditors.

4.5.1 Are pre-packs effective and for whom?

Undeniably, various advantages that emerge from pre-packs can justify their usage and their approval by certain stakeholders of the company such as secured creditors.[181] The administrator identifies the viable business parts that are sold to the new company. The liabilities are kept with the old business, apart from transferred employees who might have unpaid salaries. According to the Insolvency Service, pre-packs "may offer the best chance for a business rescue, preserve goodwill and employment, maximise realisations and generally speed up the insolvency process".[182] Cases such as *DKLL Solicitors* and *Re Kayley Vending Ltd*[183] are also contemplating the positive side of pre-packs. Nevertheless, the fact that pre-packs focus on salvaging the viable part of the business alludes that they can be ineffectual for companies with a foundational financial hardship.[184]

To undertake a pre-pack sale, the company must secure funding for the company to continue trading thus, there is no need to make the employees redundant. This means

[179] Finch, 'Pre-Packaged Administrations' (n 167).
[180] Ibid.
[181] Xie, '*Comparative Insolvency Law*' (n 172) 35.
[182] The Insolvency Service 'Enterprise Act 2002' (n 10).
[183] [2009] BCC 904.
[184] V Vilaplana, 'A Pre-pack Bankruptcy Primer' (1998) 44 Practical Lawyer 41.

that the company employees are usually secured. Frisby in her empirical research recorded that in pre-pack sales, 92 per cent of the companies kept all of their employees, whereas in normal business sales only 65 per cent of the companies transferred all of their employees.[185] The new company owners will attempt to maintain the workforce as to the extent that they consider ineluctable. Still, empirical findings elucidate that in pre-packs, employees usually keep their jobs.[186] This effect is practically influenced by Transfer of Undertakings (Protection of Employment) Regulations 2006,[187] which entails that after Brexit the aftermath will be precarious. When evaluating a certain procedure, the moral aspect has to be taken into account. One of the main reasons that pre-packs are deemed sufficient is that most of the employees manage to save their jobs.[188]

Pre-packs are speedy and not time consuming and this could prevail to be valuable since publicity is avoided. There are companies that are relying on their public perception, which means that their brand or portfolio or intellectual property assets are better to be protected. When a company with goodwill or intellectual property announces that is going through an insolvency procedure the adverse publicity could harm the company's reputation irretrievably.[189] Pre-packs can ensure the protection of the business reputation. Therefore, the depreciation of the company value does not occur during a pre-pack,[190] which gives the opportunity to companies to restructure

[185] Frisby, 'A preliminary analysis of pre-packaged administrations' (n 19).
[186] Sandra Frisby, 'Unpacking pre-packs: the story so far', Recovery (Autumn 2007) 25.
[187] Kate Creighton-Selvay, 'Pre-packed administrations: an empirical social rights analysis' (2013) 42 ILJ 85-121.
[188] Sandra Frisby, 'Judicial sanction of insolvency pre-packs? DKLL Solicitors v HMRC considered' (2008) 227 Co. L.N. 1-4; David Pollard, 'Pre pack administrations - employee and pension issues' (2010) 23 Insolv. Int. 37-42.
[189] Meeks and Meeks (n 176).
[190] Sandra Frisby, 'The pre-pack promise: signs of fulfilment?', Recovery (Spring 2010) 30; Mark Parkhouse, Kerry Scott, 'A fair deal?' New Law Journal (19 March 2009) <https://www.newlawjournal.co.uk/content/fair-deal> accessed 07 October 2019.

without harming their future trading and keeping the value of the company maximised.[191]

The cost of pre-pack is less in comparison to other procedures such as SoAs.[192] However, pre-packs might not be fruitful for unsecured creditors where there are high expenses from pre-insolvency costs and where there is a fixed charge holder with a large claim.[193] That said, they could benefit through the removal of preferential claims by the business sale. Pre-pack is not a court driven procedure whereas SoAs have to be approved by the court thus, SoAs are more expensive. While other procedures are only be available to large companies, pre-packs are accessible to smaller companies that cannot bear the costs of upstream procedures. The issue of whether a pre-pack cost should be included in the administration expenses preoccupied the courts several times.[194] According to the amended IR 2016, r 3.52, pre-appointment costs can now be considered as administration costs. Frisby stated that it is common for IPs to adopt a pre-pack strategy since when funding is not available, the company is restricted from trading.[195]

Pre-pack sales generate controversial issues since the effect is different on each stakeholder, which corresponds to the statement of interviewee 8: [196]

> "…so pre-packs are effective for the elements of the business which are profitable. Pre-packs can be positive to stakeholders such as banks, an employee group, a particular

[191] Frisby, 'A preliminary analysis of pre-packaged administrations' (n 19); *Hellas.*
[192] Graham Review (n 22).
[193] Frisby, 'The pre-pack promise' (n 190).
[194] *Re Johnson Machine*; *Kayley*; Peter Walton, 'Pre-packaged administrations - trick or treat?' (2006) 19 Insolv. Int. 113-122.
[195] Frisby, 'A preliminary analysis of pre-packaged administrations' (n 19) 72.
[196] Interviewee 8 (n 68).

kind of bunch of suppliers who are supplying to the viable part of the business."

Pre-packs have a positive impact on secured creditors as they are in a better position than when the company goes into liquidation.[197] QFCHs advantage from cheaper costs, monitoring and speedier returns.[198] Interviewee 8 above concurs with the fact that that pre-packs can indeed be more fruitful for certain stakeholders such as banks and employees. Unsecured creditors though are in the cluster of stakeholders that capture most of the burden, especially in situations where there are high costs and fixed charge holders whose credit is extensive. Therefore, when the distribution takes place – since the company funds have been diminished – there will be nothing left for unsecured creditors.[199] Frisby recorded that business sales can be more helpful for unsecured creditors than pre-packs but she concurrently stipulated that the difference is minor.[200] The quantitative data analysis of this research detected that 35 out of the 117 companies who had a pre-pack, repaid their secured creditors in full, whereas 2 out of 117 companies fully repaid their unsecured creditors. As unsecured creditors are usually in an adverse position, their condition would not have been vigorous without a pre-pack.[201] Only 6 out of 483 companies that did not have a pre-pack provided full returns to unsecured creditors. This analysis concludes that the prospects for unsecured creditors are akin even if there is a pre-pack or not. When a pre-pack did not take place, 24 per cent of companies provided a full repayment to secured creditors, whereas in pre-packs the percentage of full returns reaches the 30 per cent. These results carry the reservation

[197] Keay and Walton (n 29) 119.
[198] Louise Gullifer, Jennifer Payne, *Corporate Finance Law: Principles and Policy* (2nd edn, Hart Publishing 2015) 331-333.
[199] Van Zwieten (n 52) 478.
[200] Sandra Frisby, 'The pre-pack progression: latest empirical findings' (2008) 21 Insolv. Int. 154-158; Frisby, 'The pre-pack promise' (n 190).
[201] David Milman, 'Priority-related issues in the context of administering an insolvent estate: status quo or a new balance?' (2014) 363 Co. L.N. 1-5.

that there was not a completion of administration in some cases therefore, the distribution to creditors has not yet occurred. The beneficial effect on secured creditors has been scrutinised and characterised as biased.[202] Pre-packs are ostensibly producing the best results for most of the stakeholders but according to Milman: "…the interests of a few may need to suffer in the service of the needs of the many."[203]

4.5.2 Why did pre-packs gain a negative reputation?

Pre-packs frequently attract media, politician and creditor attention with a negative publicity. The reasons for criticism towards pre-packs include *inter alia* phoenix sales, improper use and unjust treatment towards particular stakeholders. Confidentiality issues do not allow the availability of a lot of public data on pre-packs which creates issues of opacity. Action has been taken to minimise the controversies thus, the reasoning behind the negative promotion of pre-packs is scrutinised.

Since the administrator does not have to retrieve the court's or creditors approval, there is a fear that the pre-pack might take an abusive form. Even if all or most creditors argue against the pre-pack, it turns out that the pre-pack sale might still happen.[204] The Insolvency Service stated that pre-packs can be vulnerable to abuse from directors and administrators, but this again could also be the case for any other insolvency procedure.[205] As confirmed in *Kayley*, the court has the authority to interfere

[202] Frisby, 'Judicial sanction of insolvency pre-packs?' (n 188).
[203] Milman, 'The administration moratorium' (n 108).
[204] *DKLL Solicitors*; Van Zwieten (n 52) 497-498.
[205] A recent example is *Hunt v. Michie* [2020] EWHC 54 (Ch); Peter Walton, 'Pre-packin' in the UK' (2009) 18 I.I.R. 85-108; Desmond Flynn, 'Pre-pack administrations – a regulatory perspective' Recovery (Summer 2006) 3; Anousha Sakoui, Kiran Stacey, 'Investors call for 'pre-pack' changes' Financial Times, 9 December 2008 <https://www.ft.com/content/233336d6-c57a-11dd-b516-000077b07658> accessed 7 October 2019.

if there is an obvious abuse or for any other explanation, that a reasonable person considers, that sales should not take place.

In pre-packs there are suspicions that the business is sold to the directors or previous owners.[206] In this way, the owners get back their business without the previous liabilities.[207] Lawyers state that this is indeed happening but only a small number of professionals who are characterised as 'bad professional apples' tend use pre-packs in a way that enables phoenix trading.[208] Davies mentions: "notwithstanding the considerable antipathy of both the profession and the courts towards phoenix operations, insolvency sales to unscrupulous management still occur and the pre-pack is the jemmy in the burglar's jacket".[209] This behaviour is not mainstream but Frisby's empirical analysis of 2009 suggests that 59 per cent of pre-pack sales are directly involving connected parties.[210] After the EA 2002 connected parties sales became more intense. The pre-pack pool's statistics are still in line with Frisby's statistics, since in 2018 it was indicated that 55.5 per cent of pre-pack purchases were done by connected parties.[211] The reputation of pre-packs is also harmed due to insiders who can benefit from the debt owed to unsecured creditors. The Insolvency Service Consultation of 2010 recommended that phoenix operations will be limited if pre-pack proposals required the consent of unsecured creditors and the court's before executing the pre-pack.[212] These changes would have damaged one of the advantageous features of pre-packs, which is speed.[213]

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[206] Richard Ferguson, 'A practical guide to insolvency' (2009) 9 L.I.M. 203.
[207] Ibid.
[208] Finch, 'Pre-Packaged Administrations' (n 167).
[209] Davies, 'Pre-pack' (n 177).
[210] Sandra Frisby, 'The Second Chance Culture and Beyond: Some Observations on the Pre-pack Contribution' (2009) 3 L. & F.M.R. 242-247.
[211] Pre-Pack Pool - annual report 2018 (n 21).
[212] The Insolvency Service, Consultation/Call for evidence Improving the transparency of, and confidence in, pre-packaged sales in administrations, (March 2010) 10.
[213] Walton, 'Government consultation' (n 165) 3.

The lack of transparency produces a lot of criticism on pre-packs. Ellis has suggested the following: "What we need is for responsible IPs to be bold, to have the courage of their convictions and to state publicly and transparently why the business was sold through a pre-pack without advertising or market testing."[214] The trust of creditors, customers and employees is important to be kept hence, the majority of pre-packs are negotiated in secrecy.[215] The unsecured creditors usually feel disenfranchised because there is nothing left for them.[216] The confidence of unsecured creditors towards pre-packs is therefore lost. The transparency absence consequently leads to lack of accountability. Some reviews attempted to address the issue of transparency but without substantial success.

During administration, the business is exposed to the market but pre-packs do not engage with market exposure and even if they do it would be for a short period.[217] The minimum effort of realising the business to independent purchasers creates a hostile impression.[218] Albeit, pre-packs promise the maximisation of assets, the inadequacy of marketing could reduce the business value. The confidence of creditors could be lost because limited marketing will not be in their best interests. The negative attitude of critics paired with the dissatisfaction of unsecured creditors and other pre-pack disadvantages, such as the suspicion of phoenix trading, led to the bad reputation of pre-packs.

Pre-packs' excessive criticism influenced the commencement of a review that was conducted by Teresa Graham as a wider component of the 'Transparency and Trust'

[214] Martin Ellis, 'The thin line in the sand – pre-packs and phoenixes' Recovery (Spring 2006) 3.
[215] Catherine Shuttleworth, 'Pre-packs: the latest wave of reform' (2015) 8 C.R. & I. 61-63.
[216] See Chapter 4, Section 4.2.2, Graph C; Frisby, 'Interim Report to the Insolvency Service' (n 70).
[217] Frisby, 'The pre-pack progression' (n 200).
[218] Bo Xie, 'Regulating pre-packaged administration - a complete agenda' (2011) 5 J.B.L. 513-527.

agenda.[219] Therefore, the government's interest about pre-packs can be identified through the proposals of the Graham Report. Six recommendations that were included in the review were pictured as necessary for a non-legislative process. The ministry pronounced that unless the Graham Review's findings are applied, pre-packs will be legislated.[220] After the Graham Review changes were directed at connected sales.

The pre-pack pool was the Graham Review's recommendation that was enforced in 2015.[221] It is a group of businessmen whose duty is to provide their experience and knowledge independently to parties who undertake pre-pack sales.[222] The initial step is to approach the pre-pack pool before the sale takes place, and parties reveal the agreement details. The recommendation's purpose was to tackle the lack of transparency by keeping the interested parties informed. Each application is submitted voluntarily by a connected party and reviewed by one member of the pool.[223] From the beginning the number of cases that have reached the pre-pack pool were low since in 2016, only 28 per cent of eligible companies filed their case to the pre-pack pool while in 2017, this percentage decreased to 11 per cent of eligible cases.[224] The numbers do not seem to be sanguine for the pre-pack pool as in 2018, there was a perturbing decline to 7.5 per cent.[225] What is considered as a drawback is that the forum does not address pre-pack sales to non-connected parties.[226] As the aim of the pre-pack pool was to improve the oversight of pre-packs, there were referrals of making the pre-pack pool

[219] Department for Business, Innovation and Skills. 'Transparency & Trust: Enhancing the Transparency of UK Company Ownership and Increasing Trust in UK Business', June 2013.
[220] John Wood, 'The sun is setting: is it time to legislate pre-packs?' (2016) 67 N.I.L.Q. 173-188, 174.
[221] The Pre-Pack Pool <https://www.prepackpool.co.uk> accessed 06 October 2019.
[222] Paul Dutton, Lemi McAuley, 'Addressing Concerns About Pre-packs – The 'pre-pack Pool'' Lexology, 24 March 2016.
[223] Graham Review (n 22) para.9.10.
[224] Pre-Pack Pool – Annual Review 2017, (May 2018) <https://www.prepackpool.co.uk/uploads/files/documents/Pre-pack-Pool-Annual-Review-2017.pdf> accessed 07 October 2019; The 2019 Annual Review is not available yet.
[225] Pre-Pack Pool - annual report 2018 (n 21).
[226] Milman, 'Administration under Sch.B1 to the Insolvency Act 1986' (n 83).

mandatory.[227] When the interviewees of this thesis where asked whether they believe that the pre-pack pool should become compulsory, they replied the following:

> "I think that the SIP 16 should address the connected party issue. I think creditors still feel that if there is a sale to a connected party in a pre-pack there is more noise generally around it than there is if there is a sale to a genuine 3rd party…What I would do for the pre-pack pool is that I would make it mandatory for connected parties and that has been my view for a while."[228]

> "I think that the pre-pack pool should be made compulsory over a certain level of transaction in terms of value. It should be made compulsory for larger sized businesses and reducing the fee level it will help us. The £800 plus VAT is seen as a hurdle. They may think there is no consequence for not applying and to date there are very little consequences of not applying. There are some famous cases that did not apply and no one has really bothered. The most famous name that I can recall is Jamie Oliver's restaurant chain. It should have applied to the pre-pack pool because obviously it is connected. That is frustrating for that kind to business to take that view and nobody questions it really."[229]

[227] R3, 'Government pre-pack review opportunity for improvement' (13 December 2017) <https://www.r3.org.uk/index.cfm?page=1114&element=31163> accessed 07 October 2019; Bolanle Adebola, 'The case for mandatory referrals to the pre-pack pool' (2019) 32 Insolv. Int. 71-77.
[228] Interviewee 8 (n 68).
[229] Interviewee 1 (n 145).

Since January 2019, a pre-pack sale case can be reviewed for the amount of £950 plus VAT, while before that it was £800 plus VAT.[230] Vaccari is of the opinion that the pre-pack pool should only become mandatory to medium and large companies and not micro and small enterprises.[231] This might still be a problem though since many companies are small. He thinks that it is unfair for smaller companies to pay the pre-pack pool fee, which seems to be in agreement with the views of interviewee 1 above. Even if the pre-pack pool does not continue to be optional, action must be taken that would incentivise connected parties to use it.

Threats that derive from connected party sales are an endurance of poor business models and the attempt of connected parties to buy their own economically failing business could be a sham. These connected parties might merely aim to reengineer the business by writing off a large amount from their debt. These concerns led to the addition of Article 129 of Small Business, Enterprise and Employment Act 2015 (SBEEA 2015)[232] where a part of it states the following: "The Secretary of State may by regulations make provision for— (a) prohibiting, or (b) imposing requirements or conditions in relation to, the disposal, hiring out or sale of property of a company by the administrator to a connected person in circumstances specified in the regulations." *Hunt* is an exemplary case that mirrors the aforementioned caveats. In this case the business was sold back to its director at an undervalue through a pre-pack. The director was held liable since Judge Sally Barber clarified that: "the duties owed by a director to the

[230] Pre-Pack Pool, 'Questions & Answers about the PrePack Pool' <https://www.prepackpool.co.uk/questions-answers> accessed 07 October 2019.
[231] Eugenio Vaccari, 'Pre-pack pool: is it worth it?' (2018) 29 I.C.C.L.R. 697-712.
[232] It is noteworthy to mention that the enactment of SBEEA 2015 brought more powers to the administrator. In s 117 it is stated that the administrator has the authority to take an action against fraudulent and wrongful trading which was given effect through IR 2016. Additionally, s 127 of the same act provides to the court the flexibility to prolong administrations for the maximum period of 12 months.

company and its creditors survive" when the company is insolvent. [233] It is anticipated that this case will have important implications on pre-packs in the near future.[234] Legislative action might need to be undertaken as a result, as the danger of immoderate abuse can be gleaned by the statutory change of SBEEA 2015[235] and the case *Hunt*. Yet, interviewee 7[236] also believes that excessive legislation engenders complications rather than easing the situation since he said that:

> "I think that we have far too much legislation. It is a practical issue not a legal one. It is not a question of having more rules but a question of making sure that there is compliance with the existing rules."

The three remaining experts that were interviewed in the UK expressed their opinion on whether pre-packs should be subject to a specific legislation. Interviewee 2[237] agreed with interviewee 7 in the previous excerpt by answering that:

> "By putting additional law and rules around that process I am not quite sure what that would look like and I do not think that that is necessary. On the subject of transparency, it is a double-edged sword because by making things more transparent to creditors there is a huge risk that they will just pull support anyway and the business collapses and that is why pre-packs are brought in in the first place."

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[233] *Hunt* para 60.
[234] James Hurley, 'Court ruling keeps directors on the hook after prepack insolvency' The Times, 27 January 2020.
[235] David Milman, 'Corporate insolvency in 2015: the ever-changing legal landscape' (2015) 369 Co. L.N. 1-5.
[236] Interviewee 7 (n 144).
[237] Interviewee 2 (Insolvency Practitioner), Big Four (Leeds, UK, 14 December 2018); see Appendix D.

Interviewee 8[238] thinks that the statutory action on pre-packs is unnecessary by suggesting the following:

> "If you are an insolvency practitioner it means that you are licenced, you are checked and in order to like pass the checks you have to show that you are SIP 16 compliant. So, I think that it is as near to legislation, that you can probably get. I think that if someone did a pre-pack and did not adhere to the SIP 16 and the creditors took the administrators to court, they would have a pretty good argument."

The above interviewee believes that IPs are bound by SIP 16 anyhow and that they will be scrutinised if they do not ensure that they are complying with it. He is practically saying that SIP 16 can resemble the same effect as a legislation on pre-packs. Interviewee 1[239] though, in his statement below, conjectures that if pre-packs were subject to a specific legislation the system would have been more just:

> "If the pool was mandatory and the legislation of pre-packs occurred, the system would seem to be fairer. I don't think that many people say that the system is unfair now but because of the lack of openness and transparency they are always there to believe in the conspiracy theory. What you are not told you make up."

The second recommendation is an optional 'Viability Review' that is conducted by the connected party for the new company. Connected parties in many occasions are under the impression that the new company will successfully continue the trading of the old

[238] Interviewee 8 (n 68).
[239] Interviewee 1 (n 145).

company. Walton and Umfreville in their empirical study, highlighted that when the business is sold to an independent party rather than a connected party, the prospects of the future survival of the company are increased.[240] This recommendation's purpose is to check whether the plans for the new company are viable since usually there is not a quality check. The review provides a plan on how the connected party will control the new company for the next twelve months.[241] The value of this review could potentially be extended to unconnected parties also. The plan of the new company must contain a different approach from the old company to have a better prospect of success.[242] There has been a sporadic use of the viability review since between November 2015-December 2016[243] only 37 companies filed for a viability review, while in 2018[244] there were solely 31 cases. Due to the optional nature of the viability review there is no real motivation of taking it up, which is more intense in circumstances where the directors are keen to avoid exposure.[245] The market could conceivably manipulate the purchaser's attitude. This could happen if credit managers were restricted of the finance that they were supposed to procure to the purchaser when they did not make a reference to the pre-pack pool and the viability review.[246]

[240] Peter Walton, Chris Umfreville, 'Pre-Pack Empirical Research: Characteristic and Outcome Analysis of Pre-Pack Administration' University of Wolverhampton (2014).
[241] Tom Astle, 'Pack up your troubles: addressing the negative image of pre-packs' (2015) 28 Insolv. Int. 72-74.
[242] Xie, '*Comparative Insolvency Law*' (n 172) 148.
[243] Insolvency Service, '2016 Annual Review of Insolvency Practitioner Regulation' (31 March 2017) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/605331/Annual_Review_Of_IP_Regulation_2016_final.pdf> accessed 07 October 2019.
[244] Insolvency Service, '2018 Annual Review of Insolvency Practitioner Regulation' (28 May 2019) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/807755/Annex_1_Annual_Review_of_IP_Regulation_2018_Final.pdf> accessed 07 October 2019.
[245] Wood 'The sun is setting' (n 220); Chris Umfreville, 'Review of the pre-pack industry measures: reconsidering the connected party sale before the sun sets' (2018) 31 Insolv. Int. 58-63.
[246] Stuart Hopewell, David Kerr, 'Unpacking the Pre Pack' Credit Management Magazine (November 2016) 13 <https://www.insolvency-practitioners.org.uk/download/documents/1467> accessed 07 October 2019.

The Graham Committee also suggested that SIP 16 should be redrafted in a way that the committee's recommendations would be contained in the SIP 16. The Committee detected that one of the chief disadvantages of pre-packs was the lack of good marketing of the business. According to statistics in 2007, only a small percentage of pre-packs puts the business into the market in the appropriate way, but by 2014 it had been recorded that the business in pre-packs were better marketed than before.[247] The committee's fourth recommendation was that the six good principles of marketing should be used for pre-pack sales to ensure that the appropriate marketing is taking place. Through these principles the target was to make the procedure more transparent but the concern about the sale to connected parties might remain.

The fifth recommendation entailed a suggestion to amend SIP 16 in a way that requires valuations to be conducted by a valuer with professional indemnity insurance. This recommendation was followed by a reformed SIP 16 in November 2015, which focused on making the marketing of the business sale more transparent. Therefore, an attempt to alleviate the negative criticism towards pre-packs was made through the addition of the marketing principles and valuation since it created more transparency to the pre-pack procedure.[248]

The last recommendation of the Graham Committee was that Recognised Professional Bodies should monitor SIP 16 instead of the Insolvency Service. If the administrator's professional body deals with the process it would be more accurate to the needs of the profession. However, some concerns were expressed since it is

[247] Frisby, 'A preliminary analysis of pre-packaged administrations' (n 15); Walton and Umfreville 'Pre-Pack Empirical Research' (n 240).
[248] Bolanle Adebola, 'Proposed feasibility oversight for pre-pack administration in England and Wales: window dressing or effective reform?' (2015) 8 J.B.L. 591-606; Wood 'The sun is setting' (n 220).

perceived that the Recognised Professional Bodies protect their members from adverse actions that usually come from dissatisfied creditors.[249]

The recommendations of the Graham Review were all executed which shows a genuine attempt to curtail the negative reputation of pre-packs. *Hunt* gave rise to discussions about initiating a compulsory independent panel that will have as a purpose the scrutiny of pre-pack deals. The problems during insolvency procedures will always arise since it is almost impossible to satisfy the necessities of everyone. If the pre-pack controversies remain energetic in the future though they might need to be included to the legislation.[250]

4.5.3 Comparison between pre-pack strategies and ARs in terms of a rescue agenda

In AR the receiver has the power to realise the assets of the company to acquire returns owed to the secured creditors.[251] The EA 2002 severely restricted the availability of ARs since only a closed category of companies can use it. The amendment had the purpose of limiting the vast amount of power that was given to the QFCHs, which aimed to give an adequate opportunity for companies to be rescued. This change developed administration since it made it more approachable and fostered accountability.[252] There has only been one AR case in 2019[253] and the IR 2016 cover the related issues in Pt 4. This section establishes that pre-packs and ARs are similitude in terms of rescue outcome. As it was mentioned in Chapter 4, Section 4.2.3, AR revives through objective

[249] Ibid.
[250] Subject to the May 2020 sunset clause included in IA 1986, Sch B1, para 60A.
[251] AR is akin to receivership in Cyprus hence, Chapter 5, Section 5.3 contains a further analysis of this mechanism.
[252] Rizwaan Mokal, John Armour, 'Reforming the governance of corporate rescue: The Enterprise Act 2002.' (2005) 1 L.M.C.L.Q. 28-64.
[253] The Insolvency Service Statistics 2019 (n 3).

C of administration hence, this section identifies whether AR is also hiding behind the veil of pre-packs.

Both pre-packs and ARs do not aim to save the company but to help the business to survive, while their methods of achieving business rescue are different. AR hives down the viable part of the business to a new subsidiary of the company. Hiving down is one of the most effective processes for realising assets. The receiver instead of selling the whole business, identifies the items that have a long-term possibility of survival and then sells those viable business parts to a new company.[254] Rescue through an AR happens with a business sale instead of company restructuring.[255] Pre-packs help the business to continue by making a pre-arrangement with the buyers, which has business rescue as a consequence.

If there are not any available assets, the secured creditor deals with the financing that might have negative consequences on creditors because expenditures can be relatively high. A pre-pack does not require mandatory financing, but if needed the secured creditor will have a major role here too. If funding is not available though it will not be viable for the company to continue trading thus, liquidation will be ineluctable.

A defence of AR is that it mitigates the risk of wrongful trading and that secured creditors probably receive a large amount of their money. AR seems to be advantageous for secured creditors even though it writes-off a substantial amount of the debt of the company. This happens because AR's primal purpose is to ensure that the QFCH is repaid.[256] In the 2001 White Paper it was stated that: "unsecured creditors have no right

[254] Alice Belcher, *Corporate Rescue* (Sweet & Maxwell 1997) 148.
[255] Frisby, 'In Search of a Rescue Regime' (n 52).
[256] DTI (n 9).

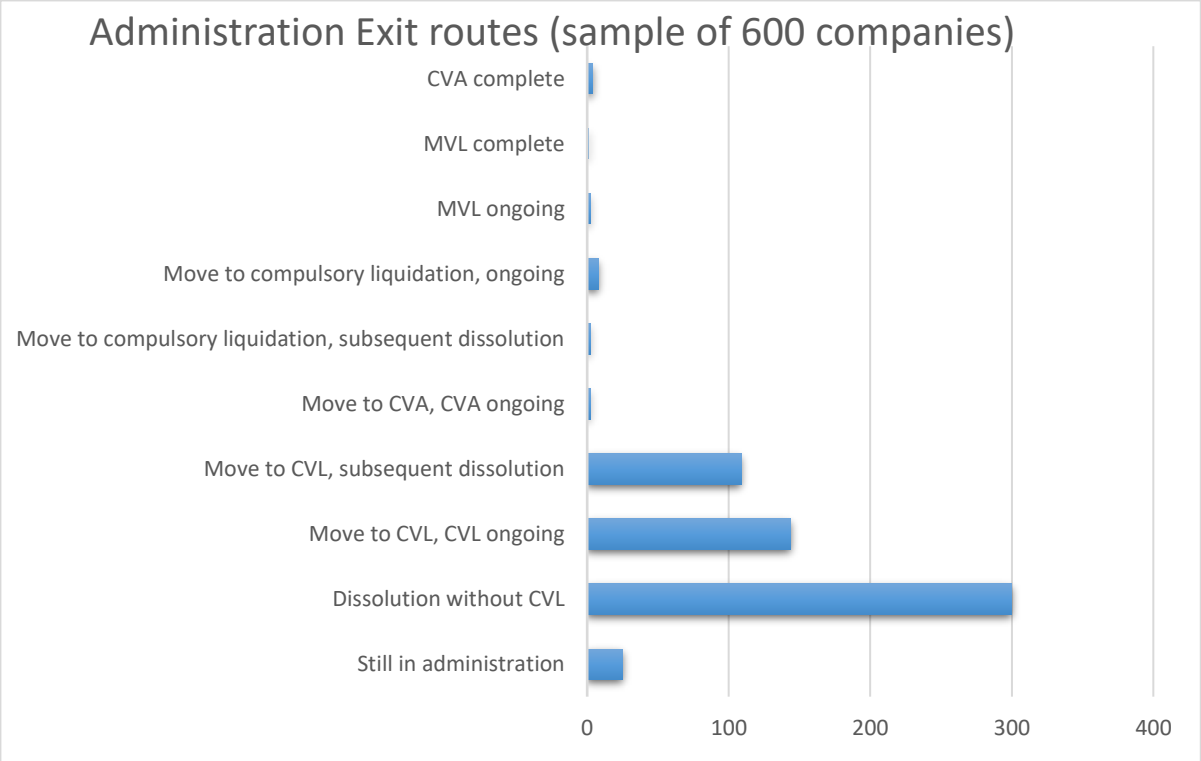
to challenge the level of costs in a receivership, even though they have an identifiable financial interest where there are sufficient funds to pay the secured creditor in full".[257] In many occasions unsecured creditors do not receive any owed debts due to the low price that the company is sold for. Both pre-packs and ARs are insolvency procedures that have an absence of collective approach during a business and/or asset sale.[258] This finding arises from the dominance of QFCHs during both processes, since they have a security over the core assets of the company, who are at the same time enjoying advance repayments.[259] ARs as well as pre-packs carry a negative reputation since they have been excoriated about their accountability and transparency.[260] The validity of the floating charge as a security device that has been critiqued.[261] This criticism is linked with the extensive control of QFCHs over the UK insolvency procedures. Ironically, secured creditors have more control in pre-packs than in ARs, since the receiver has the authority to make discretional decisions in an AR.[262] Another common ground of both procedures regarding creditors it is that is quite unusual to yield any debt returns to unsecured creditors.[263]

4.6 Exiting administration

Administration can be ceased with at least nine exit routes.[264] Some administration exit routes were explicitly stated in EA 2002 to accommodate easy exit and speed up the

[257] Ibid.
[258] Akintola and Milman (n 15).
[259] Gullifer and Payne (n 198).
[260] *Gomba Holdings (UK) Ltd v. Homan* [1986] BCLC 331; *Medforth v. Blake* [1999] 2 BCLC 221; *Silven Property v. Royal Bank of Scotland* [2004] 1 WLR 997.
[261] Statements by Lord Macnaghten in *Salomon v Salomon & Co Ltd* [1897] AC 22, 53.
[262] Walton, 'Pre-packaged administrations' (n 194).
[263] Heidi Sladen 'Tenant insolvency: pre-packs and the rescue culture: Part 4' (2011) 15 L. & T. Review 130-132.
[264] Todd (n 11).

termination of administration. These exit routes in contrast to the regime before EA 2002 obligated the administrator to finish their operations as quickly and sufficiently possible. Amongst the information that was extracted from the company documents for the qualitative analysis of this thesis were the exit routes of administration which can be seen in Graph F below. As some administrations were not completed the ongoing status of the company was recorded.



Graph F[265]

Without an extension administration is automatically terminated. The administrator vacates the office one year after administration has started, unless there has been an extension by the court or the creditors agreed to extend the administration for six months.[266] The government argued that the extension by creditors should only be for

[265] In accordance with the database of the author of this thesis.
[266] IA 1986, Sch B1, para 76-78.

three months but they were convinced that this was not practical. The court has no limitation on the period that it will allow administration to be extended.

An application can be submitted by the administrator to the court that would aim to obtain an order that will terminate administration.[267] The administrator would be allowed to follow this exit route if administration was not the appropriate mechanism for the company or because the purpose of administration was unattainable. This application could also be filed by the administrator when the purpose has been achieved.[268] After there is clear evidence that the purpose of administration has been achieved the administrator must file a notice that would require the exit from administration.[269] This reflects to IA 1986, Sch B1, para 79(3) but with the difference that this can be made without any court oversight thus, it is less expensive. The court order is required only when the administrator was appointed by the court.[270] Hence, there are occasions in which costly procedures cannot be avoided.

A creditor is allowed to make a court application in which s/he will be requesting the termination of administration on ground of improper motive.[271] According to IA 1986, Sch B1, para 85 the court must make a formal discharge therefore, this route could be an onerous burden for the court. There are occasions in which the court enforces an order for liquidating the company for the public interest.[272] The petitions are made by the Secretary of Public State in accordance to IA 1986, s 124A or Financial Services and Markets Act 2000, s 367. Where the court makes an order to wind up the company

[267] IA 1986, Sch B1, para 79(2).
[268] IA 1986, Sch B1, para 79(3).
[269] IA 1986, Sch B1, para 80.
[270] Finch and Milman, *Corporate insolvency law* (n 1) 321.
[271] IA 1986, Sch B1, para 81.
[272] IA 1986, Sch B1, para 82.

it may order the termination of administration or agree to let the procedure continue for restricted purposes.

The streamlined administration can be easily converted to a Creditors' Voluntary Liquidation (CVL) by a notice that is filed by the administrator to the Companies House.[273] This is a principal change to administration since the traditional procedure of a CVL can be avoided. This exit route can bypass the required advertisement about the appointment of the liquidator and the need to undertake a creditors' meeting. The officeholder who is recommended by the administration proposal to the creditors, becomes the liquidator of the company.[274] The documents must be sent to the Companies House at least seven days before the automatic exit from administration by effluxion of time to ensure that the administration will be converted to a CVL. As it is indicated by the above this a smart and skilful exit that had a critical role to the 2002 changes to the insolvency law. This is evidential since as it can be seen from Graph F, almost half companies move to a CVL.

If there is nothing to distribute to the creditors, the administrator must file a notice of dissolution.[275] The company is dissolved automatically 3 months after the notice was submitted. The interpretation of IA 1986, Sch B1, para 84 has triggered some uncertainties on whether this route can ever be utilised. These doubts can be contradicted though since the dissolution as an exit of administration is common since around half of the companies of this empirical research chose that route. The judge in *Re GHE Realisations Ltd (formerly Gatehouse Estates Ltd)*[276] managed to give a more rational explanation, by saying that when the administrator made all the distributions of

[273] IA 1986, Sch B1, para 83.
[274] Todd (n 11).
[275] IA 1986, Sch B1, para 84.
[276] [2005] EWHC 2400 (Ch).

the assets during administration, the dissolution of the company could be a tidier exit from the process.

The administration can come to an end when the proposals of the administrator are stalemate.[277] The final exit route that can be detected through the legislation is a court order that will take place if the administrator's actions harm the creditors or members.[278] This route is indeed avoided since Graph F indicates that only 10 companies in total moved to a compulsory liquidation.

4.7 Funding administrations[279] and administration expenses

An empirical research that was undertaken in 2000 concluded that the 75 per cent of companies that survived after a rescue process were part of an informal process.[280] The continuance of these companies happened either due to their turnaround or because they managed to receive alternative sources of finance, which helped them in discharging creditors.[281] If funding is not available in any sort of form, the only realistic option is company liquidation, since the company would not be able to bear the costs for carrying on the business and paying for any rescue procedure. A solution for saving the company is administration, which requires finance thus, if the company's cash-flow is almost non-existent, alternative sources of finance must be sought.

Creditors usually receive better returns in administration rather than liquidation but to maximise the returns funding must be available.[282] Funding can come from the

[277] IA 1986, Sch B1, para 55(2).
[278] IA 1986, Sch B1, para 74.
[279] See Chapter 2, Section 2.5 for further about SME financing.
[280] Julian Franks, Oren Sussman 'The Cycle of Corporate Distress, Rescue and Dissolution: A Study of Small and Medium Size UK Companies' (2000) London Business School.; Xie, '*Comparative Insolvency Law*' (n 172) 71.
[281] Ibid.
[282] *Re Logitext UK Ltd* [2005] 1 BCLC 326.

company's bank or from one of its major secured creditors. In other occasions though, administrators enter into factoring and invoice discounting agreements to procure funding. In these agreements the money that is raised while in administration goes to the financing company that funded the invoices. The challenge – if is that at all – is that even though the administrators get some capital upfront, any book debts would be owned by the receivables financier. Interviewee 8[283] was asked what he thinks about using factoring and invoice discounting:

> "So invoice and discounting have been very popular in SMEs for decades and I think everyone expected them to grow more than they probably have but I have just got a structured finance where they give you x percent against your receivables and they give you value against the stock in general. SMEs use it a lot, and the invoice discounting, the factoring industry has come sort of age anyway. There used to be signs that the company was weak because you had to factor your debts and your cash-flow was a problem but it is far more mainstream now so."

The above interviewee signifies that when companies procure cash-flow through factoring and invoice discounting agreements, the stigma of being in the vicinity of insolvency could be attached to them. While the use of these agreements is more common when the company has financial difficulties, this practice is now conventional even in times of prosperity. Existing security and a collateral are covering current creditors, which could encourage them to help the company. A new creditor has limited

[283] Interviewee 8 (n 68).

incentive of realising new funds though, because it is unlikely that the existing creditor will allow a new creditor to advance funds. A new financier might be reluctant to finance the company since s/he is uncertain whether the loan will be entirely repaid.[284] In these situations though, Milman and Akintola suggested that the administrator shall ensure that the existing creditors are given the "right of first refusal" as regards the financing of the company which is something that the court should consider before the liberty of actions is given to the administrator.[285]

In super-priority financing, new funders are prioritised over existing creditors.[286] In 2009, a consultation encouraged the emergence of super-priority, but those recommendations collapsed as they were never officially introduced to the legislation.[287] The super-priority of rescue finance recommendation resurfaced through the 2016 Consultation and the ICG 2018 Report of the Insolvency Service. Approximately 73 per cent of the 2016 Consultation commentators were against the proposal by stating that if the company is viable it could fund its operations without extra finance.[288] Some the 2016 Consultation respondents were concerned that the enforcement of super-priority would have a negative impact on QFCHs. A large majority of the ICG 2018 Report respondents were against these proposals, because they were of the opinion that the UK has the infrastructure for encouraging rescue finance due to where the administrations' expenses rank in terms of distribution.[289] Even if the UK does not have to comply with the EU directives in the future, there will

[284] George Triantis, 'A Theory of the Regulation of Debtor-in-Possession Financing' (1993) 46 Vand. L. Rev. 901.
[285] Sarah Paterson, 'The Insolvency Consequences of the Abolition of the Fixed/Floating Charge Distinction' (January 2017) Secured Transactions Law Reform Project Discussion series, 15.
[286] Super-priority in the USA is discussed in Chapter 6, section 6.2.3; Gerard McCormack 'Super-priority new financing and corporate rescue' [2007] J.B.L. 701-732.
[287] The Insolvency Service, Encouraging Company Rescue – a consultation, (June 2009).
[288] Peter Bailey, 'Insolvency Service publishes response to review of corporate insolvency framework' (2016) 388 Co. L.N. 1-4.
[289] ICG 2018 Report (n 140) 5.179.

certainly be an influence hence, the progress in the EU is crucial to be mentioned. Although the Directive touched upon rescue financing there are no provisions that require super-priority to be implemented.[290] In the UK currently, super-priority is only given for wages or salaries[291] but when secured assets are involved, super-priority cannot be invoked. Subsequently, a new financier is a remote possibility due to the unavailability of super-priority whereas it is more likely that an already existing creditor will provide funds over the free assets of the company or on major charged assets.[292]

The super-priority idea was influenced by jurisdictions that successfully use it, such as Chapter 11 in the USA.[293] Although super-priority was recommended by the House of Lords, it was rejected by the Government.[294] A potential route for super-priority could be IA 1986, s 19(5) and Sch B1, para 99, which cover matters on contracts about debts incurred by the administrator.[295] These contracts are prioritised over the expenses and remuneration of administrators even if it is about a floating charge. However, the definition of these sections is very broad. Arguably, super-priority is not explicitly included in the legislation, but this issue was tackled by the High Court in *Bibby Trade Finance Ltd v. McKay*.[296] As decided in this case, the new creditor's fund can be treated as an administration expense. The importance of this case is concluded on the fact that the courts are capable of authorising super-priority without any new legislation being enforced.[297]

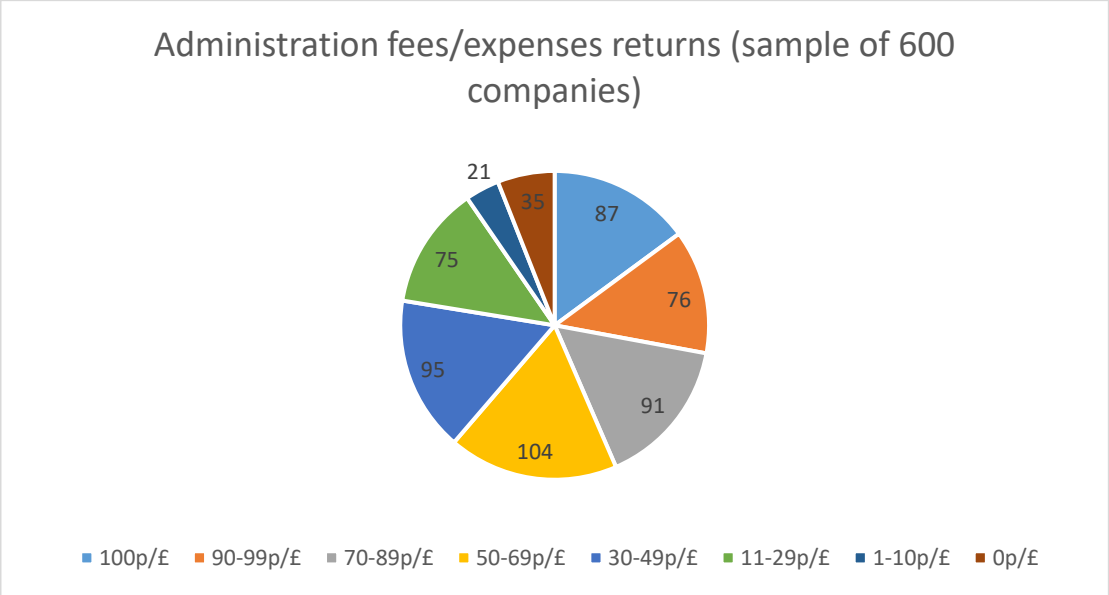
Even though administration has produced various advantages, its main problem is expenses. Costs prior to administration can be recovered, thus in many occasions

[290] The 2019 directive, Article 17.
[291] Defined by IA 1986, Sch 1, para 99(6).
[292] Van Zwieten (n 52) 545-546.
[293] Extensive analysis in Chapter 6, Section 6.2.3.
[294] Lord Hunt, HL Debates, 29 July 2002.
[295] Finch and Milman, *Corporate insolvency law* (n 1) 337.
[296] [2006] EWHC 2836 (Ch).
[297] Alistair Bacon, 'Administration Costs: Some Welcome News' (2007) 20 Insolv. Int. 1-4.

companies enter pre-packs to satisfy their need for further funding, to ensure that the company will continue operating.[298] Cases that played a vital role on addressing the issues that arise from administrations expenses are *Bloom v. Pensions Regulator*,[299] *Nortel* and *Re Game Station.* Administration costs include the administrator's remuneration and expenses, paying for the rent of the company's premises,[300] business rates regarding the company's occupied properties,[301] pension schemes and contribution notices. The expenses and remuneration of the administrator are prioritised over QFCHs claims and they are paid via their property, which they had in custody or under control before the administrator ceases the office.[302] This is a process that produces high costs since a lot of parties should be remunerated. Administration is the most profitable insolvency procedure for IPs thus, they prefer it more than other procedures.[303]Almost one in every five companies paid more than 90p in the £ for the administration expenses and the IP's fees, while less than 50 companies provided less than 10p in the £. Graph

[298] Keay and Walton (n 29) 128.
[299] [2013] UKSC 52.
[300] *Nortel case.*
[301] *Exeter City Co v. Bairstow* [2007] 2 BCLC 455.
[302] IA 1986, Sch 1, para 99(3).
[303] Elaine Kempson, 'Review of Insolvency Practitioners Fees: Report to the Insolvency Service' (July 2013) < https://www.gov.uk/government/publications/insolvency-practitioner-fees-a-review> accessed 4 October 2019.

H is a visual proof that the majority of companies do not leave the administration costs unpaid.



Graph H [304]

In *Bloom* the company received funding from the Pensions Regulator to support its entrance to administration and it was going to be treated as a provable debt which would rank as *pari passu* with other unsecured creditors.[305] It was held that this could not be the case since this kind of finance should be treated as an insolvency process expense. The following priority list was given: fixed charge creditors; insolvency procedures expenses; preferential creditors; prescribed part for unsecured creditors; QFCHs; unsecured provable debts; statutory interest; and non-provable liabilities; shareholders.[306]

After various criticisms about the excessive hourly charges of IPs for handling insolvency procedures, the Government made an announcement that the office-holders will have to give a report, which will consist further information about their estimated

[304] In accordance with the database of the author of this thesis.
[305] Peter Bailey, 'Administration and liquidation expenses and provable debts: where are we now?' (2014) 365 Co. L.N. 1-4.
[306] *Re Lehman Brothers International (Europe) (In Administration)* [2017] UKSC 38.

costs and fees.[307] The initial approach from the government was to ban time cost hence, the 2015 change was a compromise to satisfy both IPs and creditors. Thus, Insolvency (Amendment) Rules 2015 introduced the new regime on advanced fee estimates, which came into play on 1 October 2015 to deal with over-charging matters.[308] The estimation of the expenses, the reasoning for any excess expenses or charges, the anticipated remuneration of the office-holder and the constant progress reports to creditors – who have to also approve the time-cost estimate fees – are a few of the main additions of the now reconsolidated Insolvency (Amendment) Rules 2015. This change aimed to address various criticisms and to provide a fairer communication between creditors and IPs.[309]

Recouping IP fees is not always certain, thus, the participation of secured creditors is vital.[310] Although fee estimates could aid the situation, the unpredictable nature of administration should be taken into account. Creditors who are in some occasions reluctant to give their consent, must approve the estimates.[311] Therefore, if the fee estimates exceed the initial expectation it would be almost impossible to convince them to approve a further revised estimate.[312] Ultimately, it would not be in the best interests of the creditors to give their approval if the fees go beyond estimation, because it would be reduced from their returns and the result for IPs is that they might get underpaid.

Even though administration was formed in a way that facilitates rehabilitation – with the exemption of "ransom" rates – most suppliers and customers will refuse to

[307] Stephen Leslie 'Changes made to insolvency legislation on 1 October 2015' (2015) 8 C.R. & I. 210-211.
[308] The exact same rule was included in IR 2016, r.18.30.
[309] John Wood, 'Review of the regulatory system: how effective has the Complaints Gateway been?' (2017) 30 Insolv. Int. 106-113.
[310] Kempson (n 303).
[311] Chris Herron, 'The fees regime so far: the smaller firm perspective' Recovery (Summer 2017) 44.
[312] Gareth Limb, 'Upfront fee estimates in time-cost cases' Recovery (Summer 2015) 38.

interact with the company.[313] Therefore, this behaviour led to the implementation of prohibition of termination clauses through the Corporate Insolvency and Governance Act 2020 (CIGA 2020).[314] While a viable business after sale can easily obtain new funding for the company, an insolvent company's main problem is the difficulty to finance the company.[315] According to the IA 1986, the supplies to an insolvent company were restricted to water, electricity, and gas but they were extended to IT supplies via the Insolvency (Protection of Essential Supplies) Order 2015 that came into force on 1 October 2015. The continuous evolution of technology made this reform necessary since a company would be forced to close the business immediately without IT supplies.

An issue that troubled the 2016 Consultation commentators was whether the continuation of essential supplies would have a positive effect on business rescues. According to R3, the extension of essential supplies would require the introduction of a new legislation.[316] A critical concern is the scope that essential supplies should have. It would be pioneer if essential supplies could go beyond goods and services. 'Supplies' that might have an influence on the business is the prevention of the suspension of licences or trade body memberships after using an insolvency procedure. Essential suppliers will usually take control since a company that lacks cash-flow will barely be able to pay for the insolvency procedure thus, if supplies are denied a legal action against this act cannot be afforded. Invoice and discounting agreements can be valuable for a company rescue if funding cannot be obtained by any other means. However, the

[313] Jennifer Payne, 'The role of the court in debt restructuring' (2018) 77 Cambridge Law Journal 124-150.
[314] For a broad thrust of the new UK Insolvency regime see Chapter 4, Section 4.9.
[315] Shuttleworth (n 215).
[316] R3 response (n 147).

continuation of essential supplies will have an unwanted effect on the invoice finance industry due to the disturbance of contractual freedom.[317]

4.8 How administration is going to be affected by Brexit?

Administration is one of the leading rescue procedures in Europe, per the World Bank.[318] Therefore, a critical question that needs to be answered is: How will Brexit affect administration? Brexit will potentially have major consequences on the UK insolvency law in general, but the affection would also be vivid on administration.[319] Brexit will probably enhance business failures and discourage investments. On 26 June 2017, the Recast EU Insolvency Regulation 2015/848 came into force but for cases before 26 June 2017 the EC Regulation on Insolvency Proceedings No 1346/2000 will apply. Denmark is the only EU member state that opts-out of these regulations. After Brexit, the fate of administration will be uncertain since these Regulations will probably not be in effect.

The new model of administration has attracted foreign interest because it is seen as more beneficial for them than other rescue models in countries such as Germany and Spain. If automatic recognition is not still in force after Brexit it will be a hurdle for jurisdictions that would like to exploit administration. There will surely be short-term and long-term repercussions after Brexit. Milman states that: "The real joker in the pack

[317] The Insolvency Service, A Review of the Corporate Insolvency Framework response form (25 May 2016).
[318] R3, 'Brexit and the UK's insolvency and restructuring regime: The impact on the wider economy', (December 2016) <https://www.r3.org.uk/media/documents/policy/policy_papers/Brexit/R3_briefing_on_Brexit_and_the_UK's_insolvency_and_restructuring_regime_(December_2016).pdf> accessed 08 October 2019.
[319] Sonya Van de Graaff, Peter Declercq, 'What now for administrations and schemes? The Brexit fall-out' (2016) 9 C.R. & I. 174-175.

of course is Brexit which is likely to reduce inward "bankruptcy tourism" in terms of usage of administration by EU incorporated companies."[320]

Strong insolvency procedures and restructuring tools are vital as to the perception of the UK economy. This will encourage foreign companies to place their business or restructure their company in the UK. Consequently, entrepreneurship and access to credit will be improved. If the UK and the other EU member states do not agree that the UK should continue to use the EU Insolvency Regulation post-Brexit or there are no bilateral agreements between the UK and other EU member states,[321] then companies will have to rely on other cross-border insolvency mechanisms.[322] Therefore, if the negotiations between the UK and EU decide that the UK falls outside the EU Insolvency Regulations it is expected that there would be some consequences. The main impact would be on the UK economy since the Insolvency regime will stop attracting foreign companies. The automatic recognition of the insolvency processes in the UK will cease to exist in the EU and the opposite if the EU Insolvency Regulations are not applicable. The result for administration is that it will transform to a costly, lengthy and complex procedure if the interested company has assets in an EU country.[323] However, it seems that it will be to the advantage of both the UK and EU member states if an agreement that reflects a soft Brexit is formed since these EU regulations will be enforceable in the UK after Brexit.[324]

The future of administration should be decided in a way that it will not lose the attraction of foreign companies. If more jurisdictions are persuaded in using

[320] Milman, 'Administration under Sch.B1 to the Insolvency Act 1986' (n 83).
[321] About the bilateral agreements see Gerard McCormack, Hamish Anderson, 'Brexit and its implication for restructuring and corporate insolvency in the UK' (2017) 7 J.B.L. 533-556.
[322] John Wood, 'Brexit and the legal implications for cross-border insolvencies: What does the future hold for the UK?' (2017) 396 Co. L.N. 1-4.
[323] Graaff and Declercq (n 318).
[324] McCormack and Anderson (n 320).

administration it would generate engagement with lawyers, accountants, IPs as well as other parties involved in insolvency. The result would be to create more employment and eventually the economy of the country will be strengthened. Other jurisdictions give life to the UK Insolvency Law since it is already an insolvency centre for other jurisdictions. It seems that in the light of Brexit, bankruptcy tourism syndrome might completely disappear. Umfreville suggests that "the Government needs to ensure that the UK regime is as competitive and reliable as it possibly can be."[325] The competitor countries could either be Ireland owing this to their common law system or the Netherlands due to the creation of their English-speaking commercial courts.[326] Effectively, while reforming, deciding and negotiating the fate of the UK insolvency law, the needs of the global market must be uncovered.

The potential impact that Brexit will have on the insolvency regime of the UK is precarious. Only the exit negotiations could provide an answer to this controversial issue.[327] However, the above points are some possible implications that must be considered before negotiating the fate of the UK after Brexit. Even after Brexit happens, the long-term results will be ambiguous.

4.9 Conclusion: Is administration viewed as a successful procedure?

The EA 2002 aimed to enhance what the Cork Committee in 1982 wanted to achieve through the incorporation of administration. The target was to promote a rescue-oriented procedure that would facilitate the recovery of cash-flow insolvent companies. Administration was streamlined in a way that addressed several problems of the old

[325] Umfreville, 'Review of the pre-pack industry measures' (n 245).
[326] Horst Eidenmüller, 'The Rise and Fall of Regulatory Competition in Corporate Insolvency Law in the European Union' (2019) 20 European Business Organization Law Review 547.
[327] Ibid.

administration procedure. The reduced flaws of administration and the attempt to eradicate AR led to a more successful procedure than the old administration. The out-of-court appointments contributed to the increase of administrations, which reduced costs and speeded up the mechanism.[328] Albeit the costs of the new administration are less than the old administration, they are higher than AR.[329]

The moratorium protects the company from any hostile nature and gives the administrator the opportunity to concentrate on producing a plan without any interruptions. Administration is more appealing than other restructuring procedures, but sometimes the moratorium triggers the hesitation of companies to use administration.[330] Publicity could cause the downfall of the business and assets value. The fear for damaging the company's reputation resulted in the emergence pre-packs. The scrutiny of pre-packs along with other reasons such as zombie companies, high expenses and the appearance of informal procedures could be some of the reasons that led to the decline of administration.[331]

Only a minor number of companies that access administration manage to genuinely save the company.[332] Even if the company manages initially to turnaround, the empirical analysis of this research as well as another empirical study show that the majority of companies are not saved.[333] The first objective, which is to save the company as a going concern is almost never achieved but the second objective, that ensures better returns to creditors than in liquidation is efficient. In reality, there are

[328] Finch and Milman, *Corporate insolvency law* (n 1) 323.
[329] John Armour, Audrey Hsu, Adrian Walters, 'Corporate Insolvency in the United Kingdom: The Impact of the Enterprise Act 2002' (2008) 5 E.C.F.R. 148-171, 165.
[330] IA 1986, Sch 1, para 46.
[331] Finch and Milman, *Corporate insolvency law* (n 1) 324.
[332] Sandra Frisby, Report on the Insolvency Outcomes, The Insolvency Service, 2006.
[333] Ibid.

more chances in saving the business than the company.[334] A crucial factor that could be an impediment to the survival of the company and/or its business is inadequate or the absence of finance support.

The use of administration is not just for the survival of the company, but it is also utilised as an alternative to liquidation.[335] In comparison to liquidation, administration is more effective regarding creditor's dividends given that the ailing company is still in a going concern. Administration has the authority to make distributions and then directly dissolve the company with court ramification, without the additional costs that come with liquidation. However, the EA 2002 facilitates easy access from administration to a CVL. Thus, it could be more beneficial for the company to firstly go into administration and then wind up the company. In other words, even if companies are not rescued, the company is put into a more efficient liquidation.

Administration is considered as the most accountable rescue procedure in the UK, especially by creditors.[336] There is no debtor-in-possession during administration since the administrator is the only person that takes possession of the management of the company. QFCHs clearly preferred AR and campaigned aggressively to block its abolition, but now they seem at ease with the streamlined administration regime. This happens because even if administration fails, they will receive better returns than in liquidation. The statistics of the quantitative data analysis of this thesis as well as the opinion of the interviewees is extensively aligned with the literature regarding administration. As Corfield stated: "Administrations do work, but then in reality so did administrative receiverships. However, on balance, the administration process wins it

[334] Sandra Frisby, 'Not quite Warp Factor 2 yet? The Enterprise Act and corporate insolvency (Part 2)' (2007) 22 B.J.I.B. & F.L. 398-403; see Chapter 2, Section 2.4.
[335] Xie, '*Comparative Insolvency Law*' (n 171) 69.
[336] See Chapter 2, Section 2.4.2.1.

for all-round business rescue ethic, secured asset realisation, preservation of employment and maximising the return to creditors … At this point, administration is about as good as it gets." [337]

After the collapse of Thomas Cook UK Plc, the company was led into compulsory liquidation. Considering that Carillion Plc[338] and British Steel Ltd[339] also went into compulsory liquidation instead of administration generates speculation as to whether this is a new trend. These actions are questioning the effectiveness of administration and doubts are being raised as to whether administration is a mechanism that can handle large corporations. This practice is undermining administration therefore, the conclusion of this thesis highlights the rationale behind this and recommends solutions to the elicited problems.

Amid the COVID-19 outbreak the repercussions on businesses that were recently concerned healthy are inevitable. Since the lifespan of the economy are the small and medium-sized enterprises (SMEs), action needs to be taken to avoid the further destruction of worldwide and national economy. The UK legislator decided to provide further assistance to these companies through introducing a free-standing moratorium procedure, a restructuring plan procedure and the prohibition of termination clauses with the CIGA 2020. The legislator also decided to set aside temporarily the wrongful trading provisions provided by the IA 1986, s 214. This measure aims to alleviate the directors from any personal liability that they might be facing as a consequence of the pandemic. Therefore, the directors are encouraged to take risks and avoid the premature usage of insolvency procedures. Since wrongful trading provisions do not have much of an impact to the current system it is doubtful that the restriction of

[337] Corfield (n 59).
[338] The order is not available to the public.
[339] *Re British Steel Ltd* [2019] EWHC 1304 (Ch).

these provisions would achieve what is targeted. However, R3 supports that this restriction could motivate directors not to act in good faith and hence, further aid unscrupulous directors.[340]

The moratorium is a company protection of 20 days with the possibility of extending that period to 20 more days, where a monitor is appointed.[341] However, with the permission of the courts or creditors there can be a further extension which according to the legislator could take up to a year due to all of the COVID-19 restrictions. The companies cannot stop paying their debts though which is a comfort for landlords and suppliers. Companies that had problems before the COVID-19 might not sincerely want to use the procedure but take advantage of the situation. Hence, the landlords must be mindful of the history of the tenants. The moratorium propitiously addresses the *JCAM* worries of abuse. Yet, the downside is that if it fails as a procedure it could harm the reputation of the UK insolvency law regime.

The restructuring plan procedure is similar to SoAs. The differences are that the restructuring plan can cross-cram down the dissenting classes of creditors and that its availability is restricted to financially struggling companies that simultaneously have a prospect of being rescued. One of the purposes for introducing this process is to reduce pre-packs and liquidations. However, if it is only restricted to company rescue the uptake prospects will be limited.

The prohibition of termination clauses on supply contracts was a controversial change. In practice suppliers either cease supplying or threaten to stop supplying when the company is struggling as they are in excessive risk of not being repaid. If this

[340] R3, 'Suspending wrongful trading: The wrong move' 9 April 2020 <https://www.r3.org.uk/press-policy-and-research/r3-blog/more/29358/store/461237/page/1/suspending-wrongful-trading-the-wrong-move/> accessed 1 August 2020.
[341] The monitor needs to be an IP.

happens in the COVID-19 climate the failure to protect supply chain of businesses will put in danger the survival business that are viable while also putting jobs at risk. A protection for the suppliers has been incorporated by the legislator since if this obligation caused hardship to the suppliers, they could apply to the court for permission to terminate the contract. There is a possibility though that the courts will prioritise rescue over allowing the supplier to terminate. This change is contestable as it is undermining commercial contracts which would impact adversely small businesses. SME suppliers would conceivably be the most affected players. The target of these changes should be to protect companies whom their financial problems have been recent and not companies that had serious problems before the COVID-19 outbreak. These changes are certainly promoting the rescue ideology but at the same time these provisions could be feeding zombie companies.

Chapter 5 – The Cypriot Perspective in Corporate Rescue

5.1 Introduction

As a condition of the 2013 economic adjustment programme between Cyprus and the European Commission, the European Central Bank and the International Monetary Fund (Troika), in May 2015, the Parliament of Cyprus introduced the new insolvency framework for natural and legal persons. These changes targeted to modernise the laws that govern insolvency and to promote rescue culture.[1] The insolvency framework was formed with some key objectives for individuals and companies that are in financial difficulty. An objective regarding companies was to create the incentive of saving entities via implementing a formal restructuring mechanism in the legislation. Examinership subsequently emerged which aims at providing the opportunity for companies to create a plan that will facilitate debt repayment and employee preservation. Concurrently, an essential goal of the process is to keep the company value maximised since it is significant for both the company and the creditors. The incorporation of the insolvency framework into the legislation was necessary initially for political reasons and was also a foundation for creating more efficient and less time-consuming procedures.[2] The economic background of Cyprus is a factor that should be considered in the analysis. This will aid to the construction a valid conclusion about the future of these corporate rescue/restructuring procedures.

Examinership is the new restructuring tool for companies that was added to Cypriot Companies Law, Chapter 113 (CAP. 113) in 2015. Two alternative options for economically ailing companies – excluding liquidation – are receivership and Cypriot

[1] Elias Neocleous, 'Cyprus: insolvency – reform' (2015) 26 I.C.C.L.R. N85.
[2] Georgia Constantinou-Panayiotou, 'Examinership and Insolvency – New Law in Cyprus', <http://www.lawyersincyprus.com/el/article/examinership-and-insolvency-new-law-in-cyprus> accessed 10 October 2019.

Schemes of Arrangement (schemes). Schemes facilitate restructuring but through functioning differently. Both receivership and schemes could act as pre-insolvency restructuring processes since they have a business rescue angle. Simultaneously, examinership is a process that focusses on rehabilitating the entity instead of the enterprise.

After pressures from the Troika, the Cypriot legislator decided to implement examinership instead of administration.[3] Thus, a comparative approach is taken to discover whether the Cypriot legislator's decision to introduce examinership was appropriate. Although the legislator's intentions might have been genuine, this has been majorly debated. Examinership has a capability for becoming a prestigious procedure that would ease the economic struggles of companies. Yet, the current problems of examinership are overshadowing its potential. The misuse of examinership as well as other flaws undermine examinership hence, this chapter highlights the compatible solutions. According to the statistics there is some use of receivership, which shows that is preferred to examinership.[4] This chapter examines the reasons that receivership supersedes examinership.

Schemes[5] can deal with mergers and acquisitions but can also be used for rescuing companies.[6] The advantages as well as the difficulties of schemes are explored

[3] Eleni Nicolaou-Pavlidi, 'Troika rejects one out of six insolvency bills' 13 November 2014 <http://archive.phileneWs.com/el-gr/top-stories/885/227992/aporriptei-i-troika-ena-apo-ta-exi-ns-gia-tin-aferengyotita> accessed 10 October 2019.
[4] Insolvency Service, 'Statistical Data until 31 January 2016' <http://www.mcit.gov.cy/mcit/insolvency.nsf/All/9409EF9520A03E7BC2257FDA002EA577?OpenDocument> accessed 10 October 2019; 'Cyprus: Rescue procedures in insolvency' 9 September 2019 <https://www.eurofound.europa.eu/observatories/emcc/erm/legislation/cyprus-rescue-procedures-in-insolvency> accessed 16 October 2019.
[5] Schemes in Cyprus are akin to the UK Schemes of Arrangement but this procedure in Cyprus is not that attractive.
[6] Maria Kyriacou, Efrosini Monou, 'Cyprus: Overview' (10 March 2017) <https://globalrestructuringreview.com/insight/the-european-middle-eastern-and-african-restructuring-review-2017/1137882/cyprus-overview> accessed 10 October 2019.

to estimate the appropriateness of schemes for undertaking corporate rescue strategies. The insolvency framework that was introduced in Cyprus originates from the Irish insolvency framework therefore, this chapter makes references to the Irish examinership, but its further evaluation is undertaken in the next chapter.[7]

Before the addition of Insolvency Law 2015 N. 65(I)/2015 into the legislation that amended CAP. 113, Cyprus was described as stagnant regarding insolvency issues. Insolvency law in Cyprus though gradually became a substantial policy matter.[8] The average number of company liquidations during 2000-2005 was on average 324 per year but by the period of 2005-2010 there was a rise to an average of 554 liquidations.[9] By the next half of the decade the numbers increased to an average of 1638 liquidations.[10] The Insolvency Service logged a continued escalation since in 2018 and 2019 liquidations reached 2509 and 2209 respectively.[11] This can be correlated to the fact that the number of registered companies is currently not higher than 220,000.[12] While only 22 receiverships were recorded in 2009, by 2014 the number of receiverships quadrupled to 108 appointments.[13] Since the initiation of examinership in 2015 there have only been 18 cases.[14] As economically distressed companies rarely consider procedures alternative to liquidation, this is evaluated.

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[7] See Chapter 6, Section 6.3.
[8] Elias Neocleous, Maria Kyriacou 'Explaining Cyprus's attractive restructuring regime' (2013) International Financial Law Review 1-7.
[9] Insolvency Service Annual Statistics <http://www.mcit.gov.cy/mcit/insolvency.nsf/All/587242BC71DB8AE6C2257FEA0025A358?OpenDocument> accessed 03 March 2020.
[10] Ibid.
[11] Ibid.
[12] Department of Registrar of Companies, 'Companies Statistics' <https://www.companies.gov.cy/gr/%CE%B2%CE%AC%CF%83%CE%B7-%CF%80%CE%BB%CE%B7%CF%81%CE%BF%CF%86%CE%BF%CF%81%CE%B9%CF%8E%CE%BD/%CF%83%CF%84%CE%B1%CF%84%CE%B9%CF%83%CF%84%CE%B9%CE%BA%CE%AD%CF%82/?benid=1&lcyid=3> accessed 03 March 2020.
[13] Insolvency Service, 'Statistical Data until 31 January 2016' (n 4).
[14] 'Cyprus: Rescue procedures in insolvency' (n 4).

The data above suggests that the numbers are not of great importance, but for a small country like Cyprus they could be meaningful. The incorporation of modern insolvency law in Cyprus before 2015, was characterised as needless. This opinion was formed because companies that entered liquidation in the past were usually not in financial distress.[15] However, arguments prior to the banking crisis of 2013 supported that a mechanism for rescuing companies should have been formed during a prosperous era. This could have protected companies from future financial menaces. As action was not taken during a flourishing period, after the banking crisis, the rejuvenation of the law seemed imperative. An aim of this chapter is to illustrate the importance of a functional insolvency framework in Cyprus.

5.2 Economic Background of Cyprus

Cyprus is a country with a small economy, which means that most people are unfamiliar with its historical economic background hence, this thesis predicates this discussion. In 1960, the independence of Cyprus was declared by the London-Zurich agreement. The impact of English legislation is apparent in the Cypriot legislation mainly because Cyprus was a British colony. As such, the original CAP. 113 used the English Companies Act 1948 as a prototype.[16] Post-independence various factors such as manufacturing, tourism, agriculture and construction, contributed to the rapid economic development of Cyprus.[17] The Cypriot economy gradually mutated from mainly being agricultural to currently being a country with a high standard of living that relies on real

[15] Kyriacou and Monou (n 6).
[16] Kyriacos Kourtellos, Demetris Roti, 'Insolvency law reform in Cyprus – the first steps' Eurofenix (Spring 2015) 26.
[17] Central Bank of Cyprus, Athanasios Orphanides, George Syrichas (ed.), *The Cyprus Economy,* (Central Bank of Cyprus 2012) 11.

estate development, tourism and investments.[18] An evidence is the fact that in 1960 the per capita income of Cyprus was €290 and by 2016 it rose to €21,110.[19] In light of the unfortunate events that Cyprus faced since its independence, the rapid development of this country is unconventional and at the same time complacent.

In 1973 the unemployment rates in Cyprus were very low reaching 1.2 per cent of the economically active population.[20] There was also an evolution of the Gross Domestic Product (GDP) as it reached $1,066 million.[21] After a coup took place on 15 July 1974, Cyprus experienced a downfall in its development. The Turkish military took advantage of the susceptible position of Cyprus and invaded the country, which gave rise to the 1974 war between Cyprus and Turkey. Since 1974, a Green Line divides Cyprus, with approximately the 37 per cent of the north part of Cyprus being seized by Turkey. Post the Berlin Wall fall, Nicosia is now the last divided capital in Europe.[22] 46 years later the Cyprus problem is still present although numerous negotiations between Turkey and Cyprus have taken place over the years. The effect of the Turkish invasion was catastrophic for the Cypriot economy. For instance, the unemployment rates rose to 30 per cent and mass poverty conditions occurred while Cyprus was relying on other countries for resources.[23] During 1973-1975 the GDP of Cyprus dropped dramatically to 18 per cent per annum. GDP recorded a really low amount of $490 million in 1975.[24] In 1976 though, Cyprus begun to revive from the disastrous consequences that the war had caused as unemployment rates were decreasing. In 1977

[18] Costas Stamatiou, 'Cyprus's bank resolution framework: tested in the fire' (2015) 30 J.I.B.L.R. 171.
[19]Cyprus Economic Outlook, 23 September 2019 <https://www.focus-economics.com/countries/cyprus> accessed 20 February 2020.
[20] Republic of Cyprus, *About Cyprus* (Press and Information Office 2001) 150.
[21] Cyprus GDP - Gross Domestic Product <https://countryeconomy.com/gdp/cyprus> accessed 10 October 2019.
[22] Republic of Cyprus (n 20) 10.
[23] Ibid 151.
[24] Cyprus GDP <https://tradingeconomics.com/cyprus/gdp> accessed 10 October 2019.

there was an increase in the number of offshore companies hence, the same year this gave life to the offshore regime.[25] In the following years Cyprus managed to precipitously flourish from the excruciating economic circumstances that the war had left.

After several years of negotiations, the entrance of Cyprus into the European Union (EU) occurred in 2004; thus, the harmonisation of Cypriot laws with the EU legislation is what followed. When the global economic crisis started in 2008 Cyprus was minorly affected and this continued in 2009 when the recession took place. The major exposure of Cypriot banks to the Greek economy made Cyprus vulnerable and the first recession made its appearance.[26] While in 2011 the non-performing loans (NPLs) ratio was 9.9 per cent, in 2013 there was an apparent rise to 38.5 per cent.[27] The economy therefore became unstable, and the growth of economy was unmaintainable.[28] In 2013, Cyprus was in a serious economic position due to severe banking crisis that emerged. Following a request that was initiated by Cyprus to Troika, in March 2013 they agreed on an economic adjustment programme.[29] The agreement resulted in the closure and liquidation of one of the major banks of Cyprus, The Cyprus Popular Bank. The failure of a bank is considered as closely connected with NPLs of a country hence, NPLs of the banking system of Cyprus had a major impact on the banking crisis.[30]

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[25] Elias Neocleous, 'Cyprus: The Offshore Regime And Cyprus' Accession To The European Union - The Offshore Regime of Cyprus' 3 December 1997, <http://www.mondaq.com/cyprus/x/3199/Environmental+Law/The+Offshore+Regime+And+Cyprus+Accession+To+The+European+Union+The+Offshore+Regime+of+Cyprus> accessed 10 October 2019.
[26] Elias Neocleous, Maria Kyriacou, 'Cyprus: A Colonial Inheritance' 11 March 2013, <http://www.mondaq.com/cyprus/x/226084/offshore+financial+centres/A+Colonial+Inheritance> accessed 10 October 2019.
[27] Bank nonperforming loans to total gross loans (%) <https://data.worldbank.org/indicator/FB.AST.NPER.ZS?locations=CY> accessed 26 May 2019.
[28] Stamatiou (n 18).
[29] Strong Growth Prospects, July 2019 <http://www.cyprusprofile.com/en/economy> accessed 10 October 2019.
[30] Leslie Teo et al. (ed.), 'Financial Sector Crisis and Restructuring Lessons from Asia' (2000) International Monetary Fund, Occasional Paper No. 188.

According to the European Banking Authority (EBA), Cyprus is currently still the second in Europe with most NPLs, with Greece being the first.[31] EBA has logged in September 2019 that the average percentage of NPLs in the EU is 2.9 per cent and simultaneously in Cyprus the ratio reached the 21.1 per cent.[32] The agreement with Troika included the bail in of deposits that exceeded €100,000. Part of The Cyprus Popular Bank was merged with the Bank of Cyprus resulting a bank deposit levy of around 48 per cent for deposits above €100,000 in the Bank of Cyprus. All the aforesaid occurred in return for €10 billion international bailout by Troika. One of the conditions for the economic support was to modernise the Cypriot insolvency law hence, this included alterations on liquidation,[33] receivership,[34] schemes[35] and the addition of examinership to aid economically struggling companies.[36]

The economic adjustment programme came to an end in March 2016, which promoted an ambitious reform agenda and affected positively the financial stability of Cyprus. In June 2018, the cooperative bank of Cyprus collapsed although in January 2018 there was the perception that the banking system was unwavering.[37] This is a consequence of the excessive quantity of NPLs, which is a profound menace of the banking infrastructure of Cyprus that can have macroeconomic reverberations. Cyprus will be under a post-programme surveillance until no less than the 75 per cent of the

[31] European Banking Authority, 'RISK DASHBOARD-DATA AS OF Q3 2019' <https://eba.europa.eu/sites/default/documents/files/document_library/Risk%20Analysis%20and%20Data/Risk%20dashboard/Q3%202019/EBA%20Dashboard%20-%20Q3%202019%20final.pdf> accessed 20 February 2020.
[32] Ibid.
[33] CAP. 113, Part V, s 210, 212, 213, 219, 225-230, 232,235-237, 239-241, 243, 250, 251, 256, 259, 260.
[34] CAP. 113, Part VI, s 340(2).
[35] CAP. 113, Part IV, s 198(1).
[36] CAP. 113, Part IVA; David Stokes, 'Cyprus: insolvency - law reform' (2015) 30 J.I.B.L.R. N126.
[37] The Cypriot economy continues to surprise, April 2018 <https://www.hellenicbank.com/portalserver/content/atom/ba122ca0-b615-4054-878e-cf272e6e3254/content/PDF/Economic%20Research/Press%20Release%20EN.pdf?id=a7f939ea-6774-4929-8349-1c80c7df9ba6> accessed 05 June 2019.

financial assistance has been repaid. The deadline of the post-programme surveillance is in 2029.[38]

5.3 Receivership in Cyprus

The Cypriot receivership model is analogous to the administrative receivership (AR) in the United Kingdom (UK) and the Cypriot law is also following the UK concept of floating charges. The notion is identical since receivership is a procedure in which the creditors can enforce their security over the company's assets to expedite the main purpose of this procedure, which is to recover their owed debt.[39] The receiver's attempt to achieve this aim through realising the charged assets and ensuring that secured creditors receive most of their debt. Only floating charge holders – whose security usually covers most of the company assets[40] – are allowed to appoint a receiver. This makes the banks cautious as they always acquire a floating charge security to have the option of appointing a receiver if necessary.[41] The amount that floating charge holders recover depends on the value of the secured assets relative to the outstanding debt.

What makes receivership less time-consuming in comparison to other procedures – especially for the Cypriot legal framework – is that a court sanction is not required for the receiver's appointment as it can be simply done through an application to the Registrar of Companies.[42] It seems though that the directors' objections to the

[38] Post-programme surveillance <https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-financial-assistance/which-eu-countries-have-received-assistance/financial-assistance-cyprus_en> accessed 10 October 2019.
[39] Governed by CAP. 113, Part VI, s 334-344.
[40] Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 275.
[41] Paul Davies, 'Employee Claims in Insolvency: Corporate Rescues and Preferential Claims' (1994) 23 ILJ 141-169; Vanessa Finch, 'Corporate rescue: who is interested?' [2012] J.B.L. 190-212, 195.
[42] Chris Iacovides, 'Receivers and Managers' CRI Group, 3 October 2011 <http://www.crigroup.com.cy/wp-content/uploads/2018/06/Receivers-and-Managers-5-2.pdf> accessed 10 October 2019.

court defeat this purpose. Since there are no voting thresholders, the receiver can retain authority over the company promptly. The Registrar of Companies must be notified within seven days by the receiver that s/he was appointed.[43] Once the receiver is appointed, s/he must instantly inform the company since the director must send to the receiver – within 14 days – a statement of affairs that contains all assets and liabilities of the company. The appointed receiver is responsible for enforcing the security that is charged by the secured creditor, which indicates that the receiver has a duty towards that debenture holder. The duty that the receiver owes to the company and creditors falls under the law of equity.

The power to manage the company during receivership is vested on the receiver as the directors' powers cease.[44] The receiver is liable for any contracts that the company undertakes while in receivership except if the contract terms state otherwise.[45] Once the company enters receivership, the receiver's duties include *inter alia*, the issuance of all invoices, purchase orders and business letters that should have an enclosed statement of the receiver's appointment.[46] The company is not protected from hostile actions of creditors. When the company enters receivership this is publicly known, which is a fact that could harm the prospects of survival and reputation of the business. There is an upside to this though since swift decisions would have to be made and executed on the business's prospects. This could save costs and, potentially, maximise value in the context of an asset/business sale.

Once the purpose of receivership is fulfilled, a notification must be sent to the Registrar of Companies that the receiver vacated the office. This also happens when the

[43] CAP. 113, Part III, s 97(1).
[44] Kyriacou and Monou (n 6).
[45] CAP. 113, Part VI, s 337(2).
[46] CAP. 113, Part VI, s 338(1).

receiver concludes that it is not lucrative to remain in receivership. The receiver must send – within two months from the day that s/he ceased to act as a receiver – all the receipts and payments to the appointor floating charge holder, the Registrar of Companies as well as the company.

5.3.1 The effect of receivership as a corporate rescue mechanism

The company can continue trading while in receivership, but that might not have as a result the sale of the business. During receivership the discontinuance of the ongoing business operations of the company is not compulsory. The initiation of receivership can happen in conjunction with liquidation, which could have a different effect than only dealing with receivership.

Early planning is essential for the receiver's strategy to save the business. In view of this, the director should immediately provide the statements of affairs to the receiver. In due course, the receiver should decide whether to authorise the continuance of trading or whether to realise all assets or part of them instantly. Creditor or court approval is not needed, which makes the procedure speedier and less expensive than other procedures.[47] The process is expedited and minimises costs also because the primary purpose of receivership is not to save the business or a part of it.

Receivership can be combined with liquidation thus, a receiver cannot be stopped from being appointed even if the company enters liquidation.[48] That said, if rescue is attempted, it can be obstructed since the receiver cannot stop creditors from

[47] Elias Neocleous, Maria Kyriacou 'Restructuring and insolvency in Cyprus: overview' 1 March 2018 <https://uk.practicallaw.thomsonreuters.com/4-501-7673?transitionType=Default&contextData=(sc.Default)&firstPage=true&comp=pluk&bhcp=1> accessed 14 October 2019.
[48] Iacovides, 'Receivers and Managers' (n 42).

enforcing their security. Since the receiver is appointed over the entirety of a company's assets, there should be a communication with other secured creditors. Therefore, the real concern might occur where the debenture that appointed the receiver is subordinate to that of another chargee. Even if the receiver manages to sell some parts of the company business as a going concern, the prospect of survival will be probably eliminated if the company enters liquidation.[49] A moratorium is not triggered in receivership, but the company must in every invoice and purchase state that a receiver was appointed. This could harm the goodwill of the business and consequently limit chance of survival.

The interests of the receiver's appointor precede the interests of any other stakeholder. The effect on the appointor is considered before the receiver takes any actions. Receivership is inevitably mainly beneficial to a certain group of creditors. The Association for the Protection of Bank Borrowers is concerned that banks misuse receivership since limitations and/or accountability mechanisms are not in place.[50] This association also supports that the receiver's appointment causes the dissolution of the company and that unsecured creditors are left exposed. This happens because unsecured creditors rank last in terms of distribution. Also, the receiver is only obliged to protect the interests of secured creditors.[51] Interviewee 6[52] stated the following about this issue:

> "Receivership is the last resort for banks as it will try to solve the problems with the company first by trying to have a meeting to find a mutual ground between them. They will

[49] Finch and Milman (n 40) 286.
[50] Chris Iacovides, 'One Way Road to the Death of Ailing Companies – the New Receivership Bill' CRI Group, 2016 < http://www.crigroup.com.cy/wp-content/uploads/2018/06/Receivership-Bill.pdf> accessed 13 October 2019.
[51] Ibid.
[52] Interviewee 6 (Insolvency Practitioner) Big Four (Nicosia, Cyprus, 11 January 2019); see Appendix D.

> only consider receivership if the client is a bit peculiar and s/he is not willing to make a deal. Their next option will be receivership and not examinership due to the various problems this procedure is experiencing right now."

Before banks consider receivership, they offer other consensual deals to the company, which means that this tool is a way of compelling the company to make an arrangement with the bank. Debt for asset swap (dfas) can discharge debt through swapping debt for assets. This can be done through receivership but only with a compromise between creditors and debtors. Banks are in favour of dfas, as through this the NPLs issue is alleviated. The director eventually agrees since s/he has nothing else left to lose.

Receivership does not only facilitate business rescue, but also operates as a device that encourages early intervention. Interviewee 6[53] confirms this through the following comments:

> "When a receiver is appointed on a large company then other companies are afraid that a receiver might be appointed in their company too. They thought that since they appointed a receiver on that company, they might appoint one to my company. Therefore, this worked for the benefit of the banks since this resulted in rational people who made discussions with the banks to find a compromise."

Cork agreed with this view since he strongly believed that AR motivated the evasion of failure.[54] The above interviewee, as well as Cork, argue that this could aid to the creation

[53] Ibid.
[54] Sir Kenneth Cork, *Cork on Cork: Sir Kenneth Cork Takes Stock* (Macmillan 1988) Chapter 10; also see Chapter 2, Section 2.2.

of a rescue-oriented system. This opinion emerges since the mere existence of receivership and other enforcement procedures provide an incentive to preclude from using them. Contrariwise, avoidance does not necessarily promote rescue since this enticement could be given through compulsory liquidation.

The perception that the receiver's appointment is linked to company failure is maintained. This is demonstrably not the case though. In some cases, receivership can help the business to be saved but, in most occasions, this cannot be attained. Viable businesses that enter receivership can be hived down into a subsidiary company that is newly formed.[55] The subsidiary is usually sold for producing maximised returns for charge holders. Following this, the secured creditor that appointed the receiver is repaid and this process also results to the survival of the business or part of it.[56] The actual company is not saved, but parts of its business are rescued. The attempt of saving the business through a hiving down, is not a decision that the receiver is forced to take though.

Trading receivership makes the procedure lengthier, but simultaneously aids in increasing the value of the business. Hence, trading receivership can result in a business survival and at the same time secure better returns for creditors. Yet, trading receivership generates costs that can be reduced from the secured creditor's assets and put the receiver into jeopardy. The fact that the receiver can be deemed as personally liable on certain contracts can affect the returns to secured and other creditors. When Interviewee 6[57] was asked whether trading receivership is effective in Cyprus, he replied in the following way:

[55] Marcus Rea, 'Risks and Opportunities' Recovery (Summer 2017) 20.
[56] Alice Belcher, *Corporate Rescue* (Sweet & Maxwell 1997) 148.
[57] Interviewee 6 (n 52).

> "When receivership is operational, the most logical thing is that it will be time-consuming but at the same time the bank will be recovering some of its owed debt. Particularly, if the company has an income and there is a surplus then that money will be paid against the loans of the bank. Therefore, even if the assets or business are sold after 3-4 years, the bank will receive whatever was accumulated during those years. If the bank had given me another 1-2 years, I could have given them millions as the hotels that I was responsible for became really successful."

The nature of receivership would probably not allow rescue to be a frequent phenomenon. Certain circumstances must occur for rescue to be possible. The active support of the major company creditor and the restriction of other creditors from enforcing their security, are essential for a business survival.[58] Interviewee 6 is explicating that this type of receivership is long-lasting. This could, however, produce an opportunity (to the receiver) of rehabilitating a part of the business to sell at a maximised price. The receiver might have secured a certain amount of returns to the banks therefore, banks might hesitate to provide additional time to the receiver as they would not want to risk of what they have already retrieved. This reveals that business rescue is indeed happening in practice but interviewee 3[59] argues that this is not a frequent phenomenon:

> "Realistically most often by the time that companies have gone into receivership they are already deteriorated. It was

[58] Finch and Milman (n 40) 286.
[59] Interviewee 3 (Insolvency Practitioner) Insolvency Firm (Nicosia, Cyprus, 21 December 2018); see Appendix D.

> more of a matter of taking the assets and selling them. A few of the examples that we have given there have been ones where we managed to sell on parts of the business or hive it down to another company. It doesn't happen very often. Maybe a handful of cases in like 7 years I have been in Cyprus and maybe not even that many."

The two above interviewees have contradicting views on the way that receivership should be approached. While interviewee 6 said that usually his target is to bring the business back to the market, interviewee 3 said that since this is purposeless, as she usually pursues the realisation of assets through receivership. Interviewee 5[60] who has interpreted the aforementioned approaches stated the following:

> "It is a matter of culture and of the receivers themselves. We know some of them are extremely aggressive, we know X was appointed to sell them out and the business will close. If Y is appointed, he will see if it is possible to save the business and he will try."

He says that in practice receivers could either realise the assets as a piecemeal or aim for a business sale, which depends on the standpoint of the IP that is dealing with that receivership. In reality, there are receivers that do not believe in rehabilitation and that their main concern is to secure the bank's returns. If it is not into the advantage of the floating charge holder, rescue will not be even attempted. More conventionally receivership is used for generating returns to secured creditors instead of saving the company. Banks that have a floating charge over assets are usually indifferent as to

[60] Interviewee 5 (Lawyer) Law Firm (Nicosia, Cyprus, 10 January 2019); see Appendix D.

whether the business is saved, since their main concern is to receive most of the owed debt.

5.3.2 Why is receivership the dominating insolvency procedure in Cyprus after liquidation?

Ailing companies still prefer to follow receivership instead of examinership. The same happens with schemes since receivership is usually the first option of creditors who are usually holders of a floating charge. The limitations of examinership reveal the rationale behind the apathy of companies towards its usage.[61]

Even post-2015, when the IP is of the view that liquidation is not yet suitable, receivership is usually the procedure that comes to the fore. Receivership has the same negative perception that the UK AR had since it is believed that receivers sell at an undervalue, with the aim of closing down the business. The receiver has the duty of preserving the interests of its appointor. Therefore, when the assets of the company are eventually realised the employees are dismissed.

While AR post-EA 2002 in the UK is gradually disappearing, receivership is prevalent in Cyprus. Before the EA 2002, AR was the dominant procedure over administration but now things have changed.[62] This was a result of abolished AR and the streamlined administration. An empirical research illustrates that the difference between AR as it was before the EA 2002 and the streamlined administration in terms

[61] See Chapter 5, Section 5.5.2.
[62] See the archived statistics: The National archives, 'Receiverships, administrations and company voluntary arrangements in England and Wales, 1987 to present' <https://webarchive.nationalarchives.gov.uk/20140716212200/http://www.insolvencydirect.bis.gov.uk/otherinformation/statistics/historicdata/HDmenu.htm> accessed 09 December 2019.

of creditor returns and company rescue is not substantial.[63] Although, the outcomes do not have a major deviation,[64] the public is still of the perception that receivership undermines rescue culture.

As the ousted AR gave way for administration to evolve, with the abolishment of the Cypriot examinership could develop. Negative consequences can occur if the secured creditors feel that their rights have been oppressed. A problem that might be created through removing the right of the bank to appoint a receiver, is the denial of rescue funding to the company.[65] Financing the company while in economic distress is crucial for the procedure to succeed.[66] These challenges can be addressed with the rejuvenation of examinership. For instance, a power similar to Insolvency Act 1986 (IA 1986), Sch B1, para 14 could be provided to floating charge holders in examinership as they would feel that they are in more control.[67]

If banks exploit well the control that is provided to them in receivership, the realisation of assets can be executed speedily. As these creditors are in more control in comparison to other procedures, they tend to favour receivership. They also trust receivership because it is handled by licenced insolvency practitioners (IPs) who are usually experienced in the market. Court supervision is not necessary in receivership, but with an objection from the director for example, the judiciary can intervene.

This is a drawback of receivership since directors deliberately object to receivership to disturb the procedure and therefore, obstruct the control of the receiver.

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[63] John Armour, Audrey Hsu, Adrian Walters, 'Corporate Insolvency in the United Kingdom: The Impact of the Enterprise Act 2002' (2008) 5 E.C.F.R. 148-171, 165.
[64] Kayode Akintola, David Milman, 'The rise, fall and potential for a rebirth of receivership in UK corporate law' (2019) Journal of Corporate Law Studies <https://www.tandfonline.com/doi/full/10.1080/14735970.2019.1631551> accessed 29 September 2019.
[65] Iacovides, 'One Way Road to the Death of Ailing Companies' (n 50).
[66] See Chapter 4, Section 4.7. and Chapter 6, Section 6.2.3.
[67] See Chapter 4, Section 4.3.

This happens in situations where directors do not give their consent to the bank for initiating receivership.[68] This is the trivial attempt of the director to keep his/her the authority over the company. The constant contention of the procedure generates automatically higher costs and a lengthier process.[69] Interviewee 6[70] argues that:

> "When a receiver takes control there is always a reaction by the company that attempts to go to court to stop the procedure. The director of the company might block the procedure, but this is not irreversible as it can be unblocked but it is time-consuming. In my case I took control with the consent of the director and I also cooperated with him. However, when the time came to sell the hotel he blocked me, I managed to unblock the procedure and then he managed to block me again and then I managed to take control again and then with a mutual consent by the director I managed to sell the hotel."

This interviewee conveys that without the director's cooperation the procedure can become burdensome. The directors in an attempt to manipulate their position during receivership, are delaying the process in a futile manner.[71] When the business sale and/or the realisation of assets is hindered, the business and/or assets value decreases as the time passes.

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[68] *Electricity Authority of Cyprus v. Viomixania Galaktos kai Pagotou Zymaras Ltd* (2015) District Court of Larnaca, Application no: 2734/2015.
[69] Vanessa Finch, 'Re-invigorating corporate rescue' [2003] J.B.L. 527-557.
[70] Interviewee 6 (n 52).
[71] See Chapter 5, Section 5.5.2.

Yet, the procedure can also be delayed through a registration of memorandum (memo) over the company assets.[72] The court can grant an *ex parte* order that allows the registration of a memo. As a result, the realisation of the assets is restricted until the creditor that registered the memo is repaid. Occasionally, the debt to creditors is not analogous to the assets value that the memo was registered upon. As creditors abuse this given right, a recommendation would be to allow a memo only in circumstances where the debt value is half the size of the assets value.[73]

5.4 The Schemes of Arrangement procedure

Schemes[74] were copied directly from the English Companies Act 1948. Part IV was subject to a few insertions and alterations since the Companies Law enactment. Firstly, the Cypriot legislation had to be harmonised with the EU directives and regulations that lead to the addition of s 201A-201H to CAP. 113 in 2003 and the insertion of s 201I-201X to CAP. 113 in 2007. Secondly, the implementation of the Cypriot insolvency framework caused slight changes. In the legislation this procedure is mentioned as arrangements and reconstructions, but they are generally known as Schemes of Arrangement. Schemes are available to solvent and insolvent companies thus, if strictly speaking this is not an insolvency process. While in the past schemes were primarily used for cross-border mergers and acquisitions, they are now also used for debt restructuring.[75]

[72] Civil Procedure Law, Chapter 6 (CAP. 6), s 53-62.
[73] Petra Argyrou 'Hundreds of guarantors deal with memo' Sigma Live, 25 January 2017, http://www.sigmalive.com/news/local/399656/ekatontades-xiliades-eggyites-antimetopoi-me-memo> accessed 13 December 2019.
[74] CAP. 113, Part IV, s 198-201.
[75] Different restructuring regimes regulate insurance companies and banks.

Per the English precedent, it is possible to pair schemes with liquidations, administrations or examinerships.[76] Through schemes, a compromise or an arrangement can occur between the company and its creditors or a class of its creditors, or between the company and its members or a class of its members. The company, a company creditor, a company member, or a liquidator – if the company is under liquidation – can file a summary application of the compromise or the arrangement to the court which will summon a meeting.[77] The classes of creditors or members who are affected will have to be called to vote either in person or by proxy. Notices that a meeting will be held should be sent to creditors and members, that will be followed by a statement that should demonstrate the impact that the proposals will have upon them and on the directors of the company.[78] If a simple creditors' majority is obtained or members in value vote in favour of the compromise or arrangement, they are forwarded to the court for ratification. The parties of the scheme are not allowed to proceed to the implementation of the proposals without court approval. An agreed compromise or arrangement that is voted by a simple majority of the company creditors or a class of its creditors, or its members or a class of its members that has been court sanctioned is binding to all stakeholders who are affected, and even to the minority that voted against it at the meeting.[79] This means that schemes facilitate a type of cram down mechanism. The court order, approving that the company has entered a scheme, has to be registered at the Registrar of Companies and added as an appendix on all memorandum copies of the company. The value of the company might not be affected since schemes do bear

[76] Jennifer Payne, 'A New UK Debt Restructuring Regime? A Critique of the Insolvency Service's Consultation Paper - Part 2' 15 June 2016 <https://www.law.ox.ac.uk/research-subject-groups/commercial-law-centre/blog/2016/06/new-uk-debt-restructuring-regime-0> accessed 22 December 2019.
[77] CAP. 113, Part IV, s 198(1).
[78] Neocleous and Kyriacou 'Restructuring and insolvency in Cyprus' (n 47).
[79] Maria Kyriacou, *The Restructuring Review, Cyprus, Chapter 7* (4th edn, Law Business Research Ltd 2011) 82.

the perception that the company is financially distressed since it is not classified as an insolvency process.

5.4.1 The effectiveness of Schemes of Arrangement

Neocleous characterised schemes as "a very fast, simple and low cost means of restructuring".[80] He also added that if a preliminary planning is undertaken, the company can exit the procedure within a few weeks. A key element for a successful result in any restructuring/rescue process is the director's early realisation that the company is under financial difficulties. If the director takes action on time and believes that a scheme is the most suitable procedure for the current state of the company – with an experienced insolvency professional to handle the case – the company might have a reasonable prospect of survival.[81] Since schemes do not necessarily carry the perception that the company is insolvent, it might be easier for the director to decide to use schemes instead of any other insolvency procedure.

Schemes cram down the minority of creditors or members that were not in favour of schemes hence, they forced to follow the decision of the majority. The subject matter scheme, however, is subject to the court's approval to determine whether the scheme is 'fair and reasonable',[82] despite the fact that the required simple majority was satisfied. While prior to the 2015 reforms to the Cypriot insolvency regime schemes were approved with a three-quarters in value of creditors, now it changed to a simple

[80] Neocleous and Kyriacou, 'Explaining Cyprus's attractive restructuring regime' (n 8).
[81] Chris Iacovides 'Rescue Cultures', Sigma Live, 12 December 2013 <http://www.sigmalive.com/inbusiness/opinions/external/82369/koultoures-diasosis> accessed 13 October 2019.
[82] *Re Anglo-Continental Supply Co. Ltd* [1922] 2 Ch 723, 726; *Re Dorman Long* [1934] 1 Ch 635.

majority. This amendment targeted on transforming schemes into a more accessible procedure via binding the objecting parties and refraining from winding up.

The required voting in the UK schemes of arrangement are still three-quarters in majority value, which is highly criticised. Payne supports that the reduction to a simple majority would reduce the procedural requirements and subsequently schemes of arrangement will become less complicated and less onerous to handle. The fact that the 75 per cent in value of creditors need to positively vote for the procedure means that all the parties that are directly affected by the proposals need to be persuaded to agree with the scheme, which makes the procedure slow and complex.[83] In Cyprus the floating charge holder has the right to appoint a receiver instead of using any other procedure, which means that the creditors have to be convinced that the usage of schemes would produce a better results for them than receivership. With proper planning, schemes have better prospects of saving the company and/or business than receivership. At least it does not come with the stigma and value-depreciation of insolvency if it is not paired with an insolvency mechanism. Interviewee 5[84] is describing the successfulness of schemes in terms of rescue:

> "I dealt with 2 schemes. They were two companies that were in distress/insolvent. In one of the cases, the client was a developer company. The company took the money and did not manage to finish the houses due to lack of cash-flow. We went and told the buyers to give us another €20,000 each. And we explained to them that if you do not give it, this will mean that the company will go into liquidation that the bank

[83] Jennifer Payne, *Schemes of Arrangement: Theory, Structure and Operation* (CUP 2014) 192.
[84] Interviewee 5 (n 60).

> will take all of them and you will lose the €100,000 that you paid. We asked the bank to accept instalments of €500 instead of the €1000 per month that were owed … This scheme succeeded because there was a lot of preparation before we went to court to approve it."

The interviewee argues that for a scheme to have an effective outcome, negotiations must occur between the main company creditors before the case goes to the court. By elucidating to the creditors that the benefit is more perceptible if they agree to specific requirements of the scheme, the mechanism's result will be felicitous.

The Cypriot legislator decided to alter a feature of the schemes that the UK legislator is still hesitating to do. This change could cause problems to companies if they are trying to use it as a takeover or merger. Conceivably, this is the reason that the UK adheres to the 75 per cent majority. The reduction from three-quarters to a simple majority made the usage of schemes more accessible than previously but the reform was unquestionably risky, which comes with the uncertainty about the exploitation of schemes. Cypriot insolvency experts are incredulous about this reform since they argued that: "[t]he change is undoubtedly bold but it has been criticised as a charter for abuse, given the absence of an established, experienced insolvency profession and all the regulatory and other infrastructure that goes with it."[85] Arguably, after this reform one would expect that the guidance on dealing with schemes would have been established – which did not happen – hence, this creates difficulties as well as space for abuse. The fact that there is no infrastructure or a detailed guidance such as SIP in England, makes the effect of this procedure sceptical.

[85] Kyriacou and Monou (n 6).

On the one hand, there are two court hearings that are required by the law, which means that there is an extensive court observation. When the court concludes that the schemes disadvantage the minority to a great extent, the order will not be granted. This means that even though it is argued that this change would be a charter for abuse, this is mitigated due to the major court involvement. On the other hand, one could argue though that the protection of the minority is diminished because the courts and judges in Cyprus are inexperienced with matters that concern insolvency. This is also a weakness of examinership, which is analysed further.

5.5 Examinership

Examinership is a procedure that allows economically struggling companies to be restructured in order for them to be rescued. The Cypriot examinership is based on the Irish examinership that is also used for companies that are on the verge of insolvency. This section explores whether the Cypriot background was considered before implementing the Irish insolvency system in Cyprus. If the Irish examinership is not in line with the Cypriot background, even if it is successful in Ireland, the effect might not be the same in Cyprus. The opinion about the Irish examinership is controversial since statistics potentially suggest that it is a successful procedure in Ireland.[86] However, Justice Peter Kelly stated that he is hesitating to allow distressed companies to use examinership since he is supporting that usually companies in examinership are "on life support with no prospect of survival".[87] The Head of Insolvency Service in September

[86] See Chapter 6, Section 6.3; Jonathan McCarthy, 'Challenges in finding the "right" approach to SME rescue: the example of reforms to the Irish examinership process' (2019) 32 Insolv. Int. 43-55.
[87] Fiona Reddan, 'Examinership process called into question', (14 September 2009) The Irish Times <https://www.irishtimes.com/business/e xaminership-process-called-into-question-1.737567> accessed 02 March 2020.

2017 stated that there have only been nine Cypriot examinership applications.[88] These applications were either withdrawn[89] by the applicants or dismissed by the courts.[90] The reasons for the discontinuance of these cases include *inter alia*, court delays, the improper use of the process or that the requirements were not fulfilled. As Cyprus is in the EU the legislation will have to be harmonised with the directive on preventive restructuring frameworks that was enforced in 2019.[91]

One of the purposes for introducing examinership into the legislation was firstly to enable financially struggling companies to continue their business as a going concern. Secondly, the preservation of viable businesses and the restoration of their business activity. Thirdly, to obtain an economic growth and investment development in Cyprus. Furthermore, the upkeep of social cohesion and finally, the preservation of employment. The economic development and employment stability are contingent on the steadiness of macroeconomics and politics.[92] Hence, even if the ideal process is identified the economic growth of a country can be influenced, but the impact will be minor.[93]

The company, a director, a member with over 10 per cent of paid-up voting shares and a guarantor of the company are the stakeholders that can take the initiative to submit a petition of examinership to the court.[94] The moratorium[95] enhances the above aims since it gives the opportunity to the examiner to create a rehabilitation plan

[88] *Aldecor Trading Ltd v. Apostolos Marcou* (2017) District Court of Larnaca, Application no: 75/2017; *Lani Restaurants Ltd v. A&P (Andreou & Paraskevaides) Enterprises Public Company Ltd* (2015) District Court of Nicosia, Application no: 740/2015; *K.X. Peratikos Ltd v. Kyriakis Peratikos and Others* (2018) District Court of Limassol, Application no: 586/17.
[89] 'Nine applications for company examiners' (Newspaper Alitheia, 23 September 2017) 10.
[90] Ibid.
[91] Directive (EU) 2019/1023 (the 2019 directive).
[92] Richard Posner, 'Creating a Legal Framework for Economic Development' (1998) 13 World Bank Research Observer 1.
[93] Gerard McCormack 'Corporate restructuring law - a second chance for Europe?' (2017) 42 E.L. Rev. 532-561.
[94] CAP. 113, Part IVA, s 202B (1).
[95] CAP. 113, Part IVA, s 202H (1).

for the company without interruptions. Examinership requires the oversight of the courts[96] where an application with a report by an independent expert must be attached.[97] The examiner[98] is responsible for structuring a proposal that is filed to the court. This proposal consists a plan and suggestions for the survival of the company. If the court considers liquidation is in the best interests of the stakeholders, the company will not be allowed to proceed with examinership. An essential feature of examinership is that the debtor is in possession.[99] The director will have to cooperate with the examiner once s/he is appointed.[100] The examiner has the equitable right to apply to the court for removing the certain director. This happens only in situations where the director's decisions might be harmful to the company.[101] The examiner is acting as an officer of the court and not as a company agent but this changes when the powers of the director are conferred to the examiner. The directors view the fact that they are retaining control during examinership as an advantage.[102]

Examinership targets to avoid controversies with the creditors or with other stakeholders through having conventional solutions in a mutually consensual form. The examiner is also responsible for considering the broader spectrum of interests of the parties that are affected by the company failure, such as the protection of the rights of the company employees.[103] Obtaining a fresh investment for the company that needs to continue trading and fund the payments of the unsecured creditors is essential for the successfulness of examinership. The legislation provides incentives that facilitate investment attraction. For instance, the procured costs of the company during

[96] Ibid.
[97] CAP. 113, Part IVA, s 202B (3).
[98] Only a qualified IP can act as an examiner.
[99] CAP. 113, Part IVA, s 202B (9).
[100] See Chapter 6, Section 6.3.1. for a discussion on combining the control of the director with the IP.
[101] CAP. 113, Part IVA, s 202IΔ (1).
[102] Further elaboration on the DIP effect can be found in Chapter 6, Section 6.2.1.
[103] Ibid.

examinership will be included in the examinership expenses, which are prioritised over all claims except for claims from secured creditors with a fixed charge.[104] This means that it might be more beneficial for creditors to directly wind up the company rather than use examinership. A trivial rescue could drain all the available assets, that could cause a detriment further the unsecured and junior secured creditors. This chapter determines the effectiveness and successfulness of examinership with the aim of suggesting changes that would ameliorate the process.

5.5.1 The Procedure

Examinership can only be initiated if the following substantive criteria are satisfied: the company has insufficient funds to pay its debts; there is a reasonable prospect of saving the company; no resolution or order for winding up the company has been taken; the courts will not process examinership if a receiver was appointed for 30 consecutive days before the examiner's appointment.[105] If these criteria are not fulfilled and/or contravened, then the application will most likely fail at court.

Only the company, a company creditor, any guarantor of the obligations of the company and a shareholder who holds at least the 10 per cent of the share capital, can appoint an examiner.[106] This means that a shareholder minority is allowed under certain conditions to initiate examinership, even in occasions of majority opposition. If the interests of at least one class of creditors is prejudiced though, the court will not grant an approval.[107]

[104] CAP. 113, Part IVA, s 202ΛΒ (3) and (4); Georgia Mouskou, 'Amending the Companies Law to introduce a mechanism for restructuring companies and their debt' (2015) 119 ACCOUNTANCY CYPRUS 86.
[105] CAP. 113, Part IVA, s 202B (7).
[106] CAP. 113, Part IVA, s 202B.
[107] CAP. 113, Part IVA, s 202ΚΕ (4)(1)(α).

Given that the court officially appoints the examiner, s/he will have 60 days from the appointment day to create compromising and restructuring proposals.[108] Company creditors and shareholders also need to approve these proposals. Once the court ratifies the order, the arrangement has to be enforced within 30 days of the approval.[109] The court order makes the arrangement binding to all stakeholders.[110]

The examinership period is four-months with the possibility of a 60-day extension, if approved by the court,[111] with a moratorium being triggered during that time. [112] By closely studying the 2019 directive, the proposed moratorium can be paralleled with the examinership regime.[113] The time frame of four months seems tight since the examiner has only four months to get the proposals together as well as the approval of creditors. This characteristic does not leave much time for execution or testing the market.[114] Although administration has been compared to examinership, their deadlines diverge since administration can last 12 months with the possibility of extending it. As the timeframe of examinership creates obstacles, it is recommended that the deadline for larger companies should at least be altered. Interviewee 9[115] reinforces this through the following opinion:

> "In my view there should be some formula to have different time frames on larger size companies. A limit of maximum 10 or 12 months could be specified as a ceiling."

[108] CAP. 113, Part IVA, s 202IΘ (2).
[109] CAP. 113, Part IVA, 202KE (10).
[110] CAP. 113, Part IVA, s 202KE (2).
[111] CAP. 113, Part IVA, s 202H (1).
[112] CAP. 113, Part IVA, s 202IΘ (3).
[113] Mark Woodcock, '28 days later: evaluating the proposed moratorium' Recovery (Autumn 2019) 14.
[114] The deadline of the Irish examinership is compared to the Cypriot examinership in Chapter 6, Section 6.3.
[115] Interviewee 9 (Lawyer) Law Firm (Nicosia, Cyprus, 28 January 2019); Appendix D.

Interviewee 9 above suggests that the court should gain additional discretionary powers that would allow them to extend examinership. Yet, he also adds that this should only be applied in extraordinary cases, mainly due to company size.

The moratorium comes into effect once the application for examinership is filed and not from the appointment date.[116] During that period the company cannot be liquidated, a receiver is restricted from being appointed, the company property cannot be realised without the examiner's approval and the creditors cannot proceed with any actions against the company or its guarantors.[117] For instance, unsecured creditors such as water, electricity and IT suppliers cannot cease their cooperation with the company since they are obliged to continue supplying as long as the expenses are paid during the subject matter period. The examiner has the authority of not proceeding with examinership when s/he believes that the proposals are not feasible. The examiner will then have to require the directions of the court about this matter. The court can potentially order the liquidation of the company.

The court is responsible for evaluating whether "there is a reasonable prospect of survival of the company, and the whole or any part of its undertaking as a going concern".[118] According to this, rescue in examinership should be done under the current shell of the company. The main argument of chapter 2 though is that there are several difficulties in achieving company rehabilitation. This problem has already been identified in Ireland.[119]

The independent expert is responsible for revealing in his/her report whether the company has prospects of a viable future.[120] The company can either be cash-flow

[116] Mouskou (n 104).
[117] CAP. 113, Part IVA, s 202H (2).
[118] CAP. 113, Part IVA, s 202A (1).
[119] Discussed in Chapter 6, Section 6.3.1.
[120] CAP. 113, Part IVA, s 202B (4)(ε).

insolvent[121] or balance sheet insolvent[122] but at the same time it could have a reasonable prospect of survival.[123] There is a fine line between an irreversible situation and the a viable anticipation of company rescue. In *Polynikis Tourist Enterprises Ltd (HE 7795) v. Michalakis P. Charalambides and others*[124] the judge identified that the company was unable to pay its debts due to cash-flow problems. They specified that the financial difficulties of the company were temporary and that the rise of the company asset value was anticipated. In other words, even though the financial problems were apparent, the prospect of survival was reasonable. Trade ministry officials criticised this because an objective test – that can calculate whether it is reasonable to believe that the company can overcome its difficulties – is not available.[125] The judge is mainly basing this decision on the independents' expert report. If the judge decides that there is a legitimate reason for believing that a company can avoid insolvency, then an examinership order is granted. The controversial aspects of the independent expert's report are scrutinised.[126]

5.5.2 Is examinership an effective procedure for ailing Cypriot companies to survive an economic disaster?

Liquidation should be the last option for a distressed company thus, all the alternatives – including examinership and receivership – must be exhausted first. This could be

[121] CAP. 113, Part IVA, s 202A (3)(α).
[122] CAP. 113, Part IVA, s 202A (3)(β).
[123] Equivalent UK legislation about the technical meaning of these tests in IA 1986, s 123. See caution about these tests in *BNY Corporate Trustee Services Ltd v. Eurosail-UK 2007-3BL Plc* [2013] UKSC 28.
[124] (2017) Paphos District Court, Application no: 216/16.
[125] Elias Hazou, 'Examinership aimed at rescuing 'worthy' companies' Cyprus Mail, February 2015 <http://cyprus-mail.com/2015/02/03/examinership-aimed-at-rescuing-worthy-companies/> accessed 14 October 2019.
[126] See Chapter 6, Section 6.3.1 about the vitality of the independent expert's report in Ireland.

linked to the global rescue ideology whereby liquidations are stayed pending the formation and determination of viable rescue strategies. Scholars are anticipating that examinership will be used in the following years.[127]

The fact that a moratorium is in force and the director is not usually removed during an examinership suggests that examinership is debtor-oriented. This has caused repercussions to the attractiveness of examinership since Cyprus has perennially been a creditor-oriented jurisdiction.[128] This is not persuading banks to embrace examinership and simultaneously the Cypriot regime does not contain enough incentives for directors. During examinership the directors are in control, which should have emboldened them to have an early intervention. Yet, there is an apparent hesitation to utilise examinership. The Cypriot insolvency regime only penalises directors for trading fraudulently[129] not wrongfully. Interviewee 3[130] was asked whether the addition of a wrongful trading provision to the legislation could lead to more effective rescue outcomes and she replied the following:

> "I definitely think that we need something in our legislation to encourage directors to understand that there are repercussions and that they cannot hide behind the corporate veil all the time. I think that wrongful trading would be a start."

[127] Soteris Flourentzou, Evita Lambrou, 'Corporate Recovery & Insolvency 2016' (2016) Cyprus Chapter ICLG.
[128] Kayode Akintola, Sofia Ellina, 'The Use and Abuse of Corporate Insolvency Rescue Procedures: A Contextual Evaluation of the United Kingdom and Cyprus' in Jennifer L. L. Gant (ed.), *Party Autonomy and Third-Party Protection in Insolvency Law* (INSOL Europe 2019) ISBN 978-0-9931897-7-7, 137-154; Andri Antoniou, 'Examinership: A Missed opportunity' CRI Group, 24 October 2018 <http://www.crigroup.com.cy/wp-content/uploads/2018/10/Examinership-A-missed-opportunity.pdf> accessed 14 October 2019.
[129] Civil Liability: CAP. 113 Part IVA, 202ΛΣΤ; Criminal Liability: CAP. 113 Part IVA, 202ΛΖ.
[130] Interviewee 3 (n 59).

That said, if such provisions are enforced, the directors could realise that they should act promptly to avoid punishment. Alongside the company could have more chances of overcoming failure. A rigorous regime could elevate the competency of directors and potentially hold rogue directors into account when they do not consider the creditors' best interests.[131]

Although the legislator believed that this was a suitable process, the compatibility of examinership in Cyprus is questionable. Examinership is described as akin to administration but some of their characteristics are well as their outcomes diverge.[132] The Cypriot Parliament did not consider the practical issues of examinership before they decided to apply the Irish examinership directly.[133] The European Commission's statistics illustrate that the duration of court cases in Cyprus are the most extensive amongst the EU member states.[134] These delays affect the duration of cases since they are completed years after they were supposed to finish. Interviewee 4[135] who concurred with this, correlated the issue of court delays with examinership:

> "The main problem of examinership is that the Irish model has been copied in Cyprus but without taking into account the practical problems in the courts with the volume of cases.

[131] Linklaters, 'How effective is wrongful trading legislation in holding rogue directors to account' (Linklaters, May 2016) < https://lpscdn.linklaters.com/-/media/files/linklaters/pdf/mkt/london/gc6805_rogue_directors_bafs_final_a_screen.ashx?rev=8bdff673-e267-41d7-81b3-f89af822f5d4&la=jajp&hash=35FDEF13077861FAB996A77519D1A15E58132FB1> accessed 16 October 2019.
[132] See Chapter 5, Section 5.6.
[133] George Mountis, 'Appointment of an Examiner in insolvent companies' Kathimerini Newspaper, Cyprus, 19 December 2015 <http://chrysostomides.mywebreview.com/index.php?pageid=11&pageaction=chr&modid=302&pubid=33> accessed 14 October 2019.
[134] European Commission, 'The 2018 EU Justice Scoreboard' COM (2018) 364 final.
[135] Interviewee 4 (Lawyers) Law Firm (Nicosia, Cyprus, 3 January 2019); Appendix D.

> Due to the volume of cases, a case cannot be adjudicated by the court within four months."

Interviewee 9[136] who also agreed noted that:

> "The bureaucracy is an element that characterizes the whole mentality and approach on almost all matters of the Cyprus civil service causing at the end of the day considerable delays and non-effective procedures."

These interviewees underpinned that these kinds of delays operate as an impediment to the result of rescue mechanisms. As a result, court-driven procedures are time-consuming, which is a factor that negatively impacts the functionality of examinership since there is a time-limit where lawyers are forced to drop the case. This deteriorates the credibility of examinership and simultaneously discourages its usage. This also limits the probabilities of successful rescue, since if rescue is delayed the company value is deteriorated.

The first application of examinership, that the Cypriot courts dealt with, mirrors the practicality issues. The application was submitted in June 2015, but the Court's Registrar set the hearing in September 2015. Following this, the valuable time of two months was wasted hence, the viability of examinership was contested. The legislation mentions that all interested parties must be notified within three days of the petition filing.[137] A failure to comply with this, would amount to a criminal offence in which a fine of up to €5.000 can be imposed.[138] In *A&P (Andreou & Paraskevaides) Enterprises Public Company Ltd v. Lani Restaurants Ltd,*[139] the company failed to comply with the

[136] Interviewee 9 (n 115).
[137] CAP. 113, Part IVA, s 202IZ (1).
[138] CAP. 113, Part IVA, s 202IZ (7).
[139] (2015) District Court of Nicosia, Application No: 740/2015.

strict deadline and the court refused to extend it to more than three days. This is another complication that relates to the practicality of this tool since the time limit of three days to inform all the interested parties is too short. The publication of the application for informing the parties is not an option, which makes the situation even more difficult. However, if notifications to interested parties were prepared in advance, this would not have been an issue. The aforementioned case was subsequently withdrawn because there was a delay of more than three months, where the courts did not even commence the hearing.[140]

If the involvement of the court in examinership is limited, the mechanism could become speedier and less expensive.[141] The court delays make the four months of examinership too short since the examiner might need more time to finalise his/her plan. Creditors are not called to approve examinership because the procedure gets stuck at court. It is plausible that an examinership case will be subject to failure when there is lack of preliminary preparation. Planning before officially making an application to the court is valuable due to the backlog of the judiciary. Even though there is no rule that prohibits pre-packs in the Cypriot insolvency regime, there is no attempt of using them.[142] Therefore, the solution to the proposal delays of this mechanism could be to have a pre-pack in advance since it facilitates a quick business sale. This can only happen though if the legislation is altered in a way that business sales are allowed through examinership. If the regulation of this matter is neglected though, the reputation and the trustworthiness of the Cypriot insolvency regime could be jeopardised even further.

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[140] Mountis (n 133).
[141] As discussed in Chapter 6, Section 6.2.1 court supervision and the involvement of the examiner increases the costs.
[142] Elias Neocleous, Maria Kyriacou, *Corporate Recovery & Insolvency 2014 – Chapter 12 Cyprus* (8th edn, Global Legal Group 2014) 69.

Auditors or IPs can act as independent experts. A duty of good faith is imposed on the independent expert regarding the report that accompanies the examinership petition. Despite this, safety regulations that could restrict the biased behaviour of independent experts are not currently in force. An independent expert in *Peratikos* formed a report that had unrealistic assumptions. The report said that the company had prospects of survival if a loan of €1,8 million was secured and if a substantial amount of debt was written off. The challenge is to ensure that the independent expert acts in accordance with justice, not subjectively and not in favour of the company who appointed him/her. In Ireland the Specific Best-Practice Directives prevent the independent expert's prejudice while in Cyprus there is not something similar.[143] In effect, this matter can be regulated in Cyprus through the implementation of best practice guidance. This will optimistically mitigate biased practices.

Specialist courts on insolvency matters are non-existent[144] and there are no expert judges for financial issues in Cyprus.[145] The independent expert's report has amongst other things, an estimate of the long-term endurance of the company and how to attain this.[146] Usually it will not be within the expertise of the judiciary to undertake a balance sheet or a cash-flow test that determines whether the company has a prospect of survival. As a result, they tend to place extensive reliance on the independent expert's report.[147] This report is important for judges since it aids them in deciding on whether to approve the examinership petition or not. As the report is not binding, the court has

[143] Mountis (n 133).
[144] Gerard McCormack, Andrew Keay, Sarah Brown, *European Insolvency Law: Reform and Harmonization* (EE Publishing 2017) 89, 90, 100.
[145] Maria Kyriacou, 'Cyprus: New insolvency laws' Eurofenix (Summer 2015) 44; see Chapter 6, Section 6.3.1. for a discussion about the Irish courts during examinership.
[146] CAP. 113, Part IVA, s 202B(3), (4); Demetris Loizides, 'Cyprus law: Amendments introduce examinership' Harneys, 2015 <http://www.mondaq.com/cyprus/x/405708/Corporate+Commercial+Law/Amendments+To+Cypriot+Companies+Legislation+Introduce+Examinership> accessed 13 October 2019.
[147] Kyriacou, 'Cyprus: New insolvency laws' (n 145).

the discretion of deciding whether to follow it. However, there is something to be said about the fact that this is a commercial judgment and courts of law are not best placed to make this.[148] In the UK case *Re Charnley Davies (No 2*),[149] the courts were unwilling to interfere with commercial decisions of directors or office-holders. The claim against administrations as per IA, Sch B1, para 74 in case of *Davey v. Money*[150] also failed. In *Re Meem SL Ltd; Goel v. Grant*[151] the court clarified that the judiciary intervention is not only allowed in differential treatment cases but also in cases where perversity can be proved. The high failure of challenges launched by debtor interests shows that this attribute is ineffective. In *Brewer v. Iqbal*[152] the decision of Judge Briggs deviated from previous approaches as it was held that since the IP was in breach of fiduciary duty, he had to compensate the applicant. However, the general perception is that the absence of judicial financial knowledge may lead to a false decision since the judge might not be able to comprehend whether the company has a legitimate reasonable prospect of survival. The IA 1986, Sch B1, paras 74-75 have a minimal impact in bringing justice since the commercial judgment of the office-holder is conventionally not set aside. However, in cases like *Top Brands Ltd v. Sharma*,[153] the commercial judgment of the IP was disregarded as there was evidence that there was a breach of fiduciary duty of the liquidator subject to IA 1986, s 212.

The Cypriot Parliament has recently passed a bill on creating Commercial Courts in Cyprus.[154] Yet, it remains to be seen whether this is going to positively affect

[148] Andrew Keay, Joan Loughrey, 'The concept of business judgment' (2019) 39 Legal Studies 36-55, 41.
[149] [1990] BCLC 760.
[150] [2018] EWHC 766 (Ch).
[151] [2017] EWHC 2688 (Ch).
[152] [2019] EWHC 182 (Ch).
[153] [2014] EWHC 2753 (Ch).
[154] Jean Christou, 'New bill to establish commercial and admiralty courts' 6 May 2019 <https://cyprus-mail.com/old/2019/05/06/new-bill-to-establish-commercial-and-admiralty-courts/> accessed 15 September 2019.

examinership. The fact that the judiciary lacks expertise on commercial matters transmits a perception of untrustworthiness of the Cypriot insolvency regime. The introduction of mandatory training for judges could be a solution, but there have been contrasting views that doubt the adequacy of a training:

> "I don't think that a judge who is trained in insolvency procedure is the best person to decide how to deal with the business of a company with financial difficulties or a company which is insolvent. That is a job that is best carried out by a businessperson, somebody who is trained in those sorts of issues … It is a different job that needs different skills and lawyers don't have the right skills."[155]

The necessary foundation for accepting the procedure was not developed in advance and this is demonstrated by the fact that IPs are uncomfortable with using examinership because they are not familiar with it. It is difficult to change the perception of a procedure but not impossible therefore, the proper promotion should occur for the mechanism to become active. The attitude of banks and courts towards examinership does not produce favourable results for the procedure's progress.[156] Creditors are suspicious and therefore, hesitating and avoiding to use examinership. Banks are in preference of alternative mechanisms when intervention is necessary. The problems that arise from examinership need to be solved through various steps such as building an infrastructure for banks to accept this mechanism.

[155] Interviewee 7 (Lawyer/Academic) a law firm and a UK university (London, UK, 15 January 2019); see Appendix D.
[156] The importance regarding the standpoint of banks towards rescue procedures is underpinned in Chapter 2, Section 2.4.2.1.

As examinership can an expensive and an intensive procedure it needs to be supported by adequate credit. Thus, another impediment that could limit even further the usage of examinership is the unavailability of rescue finance. If the company is unable to fund the procedure this means that funding must be pursued for current or new creditors. Without incentives in place creditors are not going to be willing to finance a company as they would probably consider it as a lost cause. The legislator needs to consider ways that would encourage current and new creditors to provide such funding.

There was a rescue vision with the implementation of this tool to the Cypriot legislation. Company rescue though is considered too optimistic nowadays since there are several thresholds that need to be satisfied in order to achieve this.[157] Since examinership is already experiencing various problems, rescue is a difficult, if not an impossible target. However, a tool should be available that would be able to promote the best interests of most stakeholders. Receivership is preferred by the banks since the primary purpose of that procedure is to repay the floating charge holders whereas in examinership other aspects are also taken into consideration.

If drastic changes are not applied, examinership is doomed to fail. Another procedure such as administration could have adjusted more easily in the Cypriot legal environment. An analysis on whether administration is more efficient is an important aspect to the conclusions of this thesis.[158] However, given the above limitations examinership is in danger of being exposed to an abusive treatment, which is the next issue that this chapter focusses on.

[157] See Chapter 2.
[158] See Chapter 5, Section 5.6.

5.5.3 Is examinership misused?

Examinership aims to recover companies from economic debt hence, the intention of the legislator was generally but the framework that governs examinership gives space for unintended or intended abuse. Interviewee 4[159] stipulates that:

> "Although this mechanism had a positive intention it did not deliver as expected."

A mitigating aspect that should be considered is that law-making is difficult and therefore, it frequently creates many ambiguities. Arguably, if the procedure is easily abused it would be an addition to the above problems that would result in the deterioration of the reputation of examinership. Will the reduction of the deliberate exploitation of examinership be a steppingstone for developing a more popular and efficient procedure?

A basis for avoiding abuse was arguably built by introducing the IP profession.[160] Although an IP is considered as an expert who is responsible for undertaking examinership cases, this mechanism is occasionally not used for its envisaged purpose. If a receiver has been appointed for less than thirty continued days, once an examiner is appointed the receiver ceases to act.[161] There were cases where companies instead of genuinely utilising examinership, they used it as a defence to receivership.[162] In *Polynikis* the directors of insolvent companies that had a receiver appointed tried to frustrate receivership with examinership. Interviewee 3[163] agrees that this is frankly an issue of concern:

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[159] Interviewee 4 (n 135).
[160] CAP. 113, Part IVA, s 202ΛA.
[161] CAP. 113, Part IVA, s 202H (1).
[162] This has also been an issue in Ireland even though the space that is given is three days instead of thirty days; See Chapter 6, Section 6.3.1.
[163] Interviewee 3 (n 59).

> "… so unfortunately, the applications have been made as a way to cause problems and obstacles for the receiver rather than run genuinely in an effort to save the company. Often the court is finding that the application is made as an abuse of process and not actually with genuine effort to take forward and restructure the company."

The purpose of the directors was possibly to find alternative solutions that would help the company, but this could be a nugatory delay that is demeaning the price of the assets and/or business of the company. Most examinership cases in Cyprus had a director who was moving with urgent haste to dismiss the receiver and thus, there was not time for the preparation of the independent expert's report, even though this is required. The devious strive of the director to stop the receiver can be seen by the fact that the petition was filed to the court without the report.[164] Unfortunately, this characteristic serves as the factor that possibly vitiated the reputation and trustworthiness of the Cypriot examinership.

According to the Irish case *Re Traffic Group Ltd*[165] "It is not designed to help shareholders whose investment has proved to be unsuccessful". If the purpose of using examinership is for the moratorium for the short-term, what will usually follow is the winding up of the company. By following both procedures intentionally, more costs are generated that are extracted from the company assets therefore, the amount of distribution to creditors would be less.[166] Examinership must only be followed in circumstances where the predicted result would be better for creditors and shareholders

[164] *Kypros Kourousi and Others v. Capital Accommodation (Cyprus) Ltd* (2018) District Court of Paphos, Application no 217/2017.
[165] [2008] 3 IR 253.
[166] Jennifer Payne, 'The role of the court in debt restructuring' (2018) 77 Cambridge Law Journal 124-150.

than in liquidation.[167] Insolvency experts in Cyprus support that examinership is a tool that does not advantage the company or its creditors.[168] Particularly, a Cypriot IP stated:

> "From practical experience of the lengths directors will go to ensure their company remains in their control, despite its viability, the only people who stand to gain from this process will be the lawyers appointed to petition the court, the accountants instructed to prepare the Independent Accountant's Report and the IPs acting as examiners, definitely not the creditors or the shareholders. Not only will the cost of initiating examinership further burden an already ailing company but, in my professional opinion, this process will serve as a tool to abuse the system."[169]

There is an interim moratorium that lasts no more than 15 days, which provides time to the independent expert to submit the report.[170] *JCAM* could be used as a precedent for the Cypriot courts to tackle any relevant abusive attempts. [171] A major problem might be that even though there is a code of ethics for IPs, it is quite general and it does not provide guidance as to how they should handle certain situations. [172] A guidance equivalent to the UK Statement of Insolvency Practice could be a solution that would enhance the rectitude of the system. These statements should include guidelines for IPs

[167] CAP. 113, Part IVA, s 202B(4)(ζ); *Andrea Georgiou v. Re LND Estates Ltd* (2017) Supreme Court of Cyprus, Application No 123/2017.
[168] Andri Antoniou, 'Examinership: Potential for Abuse' CRI Group, 17 December 2014 <http://www.crigroup.com.cy/articles-publications/articles-reports/page/2/> accessed 17 October 2019; Mountis (n 133).
[169] Antoniou Ibid.
[170] CAP. 113, Part IVA, s 202Γ (2).
[171] About the improper use of the administration moratorium see Chapter 4, Section 4.4.2.
[172] Maria Kyriacou, 'Bolder and Better?' Recovery (Autumn 2015) 29.

about dealing with insolvency procedures and set the boundaries that would force IPs to act professionally.

Examinership could transform into a more successful process only if it is subject to alterations since it currently gives space for manipulation. While there are advantages in having the out-of-court examinership option, there are situations where examinership is cunningly used and subsequently, it might be more appropriate to have the court's active involvement in some situations. Furthermore, the legal opinion reinforces these views since Mountis stated the following: "In the light of the above, the first signs indicate that examinership may not serve the purpose for which it was voted, while the risk remains that it may be used as a tool for abuse rather than rescue."[173] It can be argued that administration is a more compatible procedure for the Cypriot legal system thus, this argument requires further analysis.

5.6 Would administration be a more effective procedure in Cyprus than examinership?

Commentators constantly correlate examinership to administration,[174] but it is arguably more similar to company voluntary arrangements (CVAs).[175] It seems that both CVAs and examinerships facilitate company rescue, which is closer to CVA since administration admits other types of rescue outcomes. In examinership a moratorium is involved and likewise in CVAs there is a moratorium available but only for companies that satisfy specific criteria.[176] The minority of creditors can be crammed down by the

[173] Mountis (n 133).
[174] Stokes (n 36); Kyriacou, 'Bolder and Better?' (n 173); Neocleous (n 1).
[175] For a discussion on CVAs see Chapter 3.
[176] IA 1986, s 1 and 1A.

courts in examinership as long as they consider it just and equitable.[177] Uncommonly the judiciary is involved in a CVA,[178] and only unsecured creditors can be crammed down when the plan is just and equitable as it happens in examinership. The director's authority does not cease in either examinership or CVA and there is an examiner and a supervisor/nominee[179] appointed respectively. An exegesis as to whether administration could be a better fit to the Cypriot insolvency regime is undertaken since administration deviates on many levels from examinership.

Before enforcing examinership in Cyprus, there was a dilemma on whether to introduce examinership or administration. Troika officials were under the impression that examinership would be more suitable for Cyprus thus, this potentially led to the decision of Troika to reject administration and promote examinership instead.[180] Iacovides depicted that the Cypriot insolvency framework is "at its stone age" because instead of introducing administration which he considers a more sophisticated tool for companies, examinership was implemented.[181] A comparison between examinership and administration could lead to a conclusion about the optimum adoption of rules.

The aspect of legal transplants should also be observed to evaluate whether any procedure could work more effectively in Cyprus. An important part of rescue culture is the fact that it is a 'culture'. Cultures cannot be forced on jurisdictions, but they can merely evolve over time. It is common to borrow rules as most regimes have been borrowed or at least influenced by a certain country.[182]

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[177] CAP. 113, Part IVA, s 202KE (4)
[178] Insolvency Act 2000, Sch 2, para 3 where the nominee can be substituted by the court.
[179] IA 1986, s 7(2).
[180] Chris Iacovides, 'The Irish model of "Examinership" Prevails over the English "Administration"' CRI Group, December 2014 <http://www.crigroup.com.cy/el/articles-publications/articles-reports/page/2/> accessed 14 October 2019.
[181] Iacovides, 'One Way Road to the Death of Ailing Companies' (n 50).
[182] Alan Watson, *Legal Transplants: An Approach to Comparative Law* (2nd edn, The University of Georgia Press 1993) 95, 107.

The English legislative colonial inheritance in Cyprus is apparent and can be seen in several sectors of Cypriot legislature. This is a proof that legal transplantation from the England to Cyprus is possible. That legislation that was once incorporated in Cyprus from England is no longer identical since there have been changes in both jurisdictions. The result of the operation of the laws might be different from the expectation and the intention that was once in place when transplanting the legislation.[183] However, the ensuing development of the legislation is not necessarily rejecting the transplantation.[184]

Since most examinership rules abide by the old-style administration pre-EA 2002, similar amendments could make examinership more accessible. Hence, examinership could become more attractive if the rescue outcomes turn out to be more effectuate. Would the aftermath be more fruitful if administration is directly transplanted instead? If there is a constant change in the mechanism options that are provided by the legislation, this could lead to the depreciation and the loss of veracity of the Cypriot insolvency regime.

Arguably, direct legal transplantations can easily fail when they are not compatible with the approaches of that particular country. This thesis is not questioning whether legal transplants are feasible but whether they can be operational in the subject matter country.[185] An example that arises from the findings of this thesis is the fact that the Irish examinership was basically transplanted in Cyprus and now it is gradually disappearing. As argued further, administration could have been more compatible with the Cypriot background and infrastructure. However, there are some reservations about

[183] Mohammad Rizal Salim, Phil Lawton, 'Law in a Post-Colonial State: The Shareholders' Oppression Remedy in Malaysia' (2008) *Global Jurist* (Berkeley Electronic Press) 21.
[184] Watson (n 182) 27.
[185] Ibid.

directly introducing administration to Cyprus. Perhaps it is better to use the UK corporate rescue regime as an example for Cyprus and then work from there. Certain amendments might be needed for the regime to work effectively in Cyprus. These changes do not have to do with the legal transplantation, but the functionality of the actual system which is obstructing the development of corporate rescue. The only way that the transplant could operate effectively is through allowing the rules to evolve in accordance with the background attitudes of the host country. That said, the use of examinership could increase and become a more effective process for Cyprus as systems adapt and procedures are cyclical in terms of utility.

Miscellaneous factors contributed to the underusage of administration prior to its amendment. After the EA 2002, AR was practically eradicated where administration became the leading procedure. During an amendment, the primary aim of the legislator should be to ensure that the interests of secured creditors are not harmed. The creditors are important actors in saving the company since if they do not cooperate the chances of survival would be limited.[186] Floating charge holders were discontented due to the fact that their right to appoint an administrative receiver was forbidden. The legislator considered the negative reaction of floating charge holders before introducing the EA 2002 as it gave the ability to floating charge holders to appoint an administrator out-of-court and created the three hierarchical objects.[187] Examinership has some restrictions regarding rescue since in contrast to administration there is not a business rescue angle.[188] Hence, if a company enters examinership when company rescue cannot be achieved this would mean that the company will have to go into liquidation with the

[186] See Chapter 2, Section 2.4.2.1.
[187] See Chapter 4, Section 4.2 and 4.3.
[188] The effect of this restriction is discussed in Chapter 6, Section 6.3.1.

value of the assets decreased. When interviewee 6[189] was asked whether objectives equivalent to administration – that would allow business rescue – should be introduced in Cyprus, he argued the following:

> "The same thing can happen with receivership … For example, in one case I could have told the bank that it is in your best interests to close the hotel today and sell it as it is not operational at the moment…Me along with my team, we managed to fix the results of the hotel by almost 100 per cent. We also managed to sell it at a price that was over the open market value for the period. If the bank had let me to operate it for another year I could have sold it for even more…So the second objective of administration can be achieved through receivership."

This interviewee was wondering whether it would be superfluous to alter examinership in a way that would allow a business sale since this can be done through receivership. A middle ground solution could be to streamline both examinership and receivership as it was made with AR and administration in the UK. The resemblance of AR and the streamlined administration is acknowledged and at the same time criticised by various commentators.[190] Therefore, the Cypriot legislator should be cautious of this. Since a company in receivership is not necessarily trading and there is the public perception that once a receiver is appointed it will be the end of the company, it might be difficult

[189] Interviewee 6 (n 52).
[190] Stephen Davies (ed.), *Insolvency and the Enterprise Act 2002* (Jordans 2003) 40; Gerard McCormack, 'Control and corporate rescue - an Anglo-American evaluation' (2007) 56 I.C.L.Q. 515-551; John Willcock, 'How the Banks Won the Battle for the Enterprise Bill' Recovery (June 2002) 24-26; Akintola and Milman (n 64); See also Chapter 2, Section 2.4.2.1 and Chapter 4, Section 4.2.3.

in terms of culture to classify it as a tool that pursues rescue. The opinion of interviewee 5[191] concurs with this since he commented the following:

> "More importantly, it is a matter of culture to pass on to society or to business owners."

Even though the abolition of AR assisted the promotion of administration, other amendments also contributed evolution of administration. It was streamlined in a way that gave the option to companies to appoint an administrator out-of-court but also kept the option of appointing an administrator through court. This option gave to companies the opportunity of initiating an administration that was less cumbersome and costly. The fact that an examiner can only be appointed by the court creates the same complications that the old-style administration was experiencing. If an out-of-court examinership is provided, companies could be keener on utilising examinership. However, the current caveats regarding the e-filing issues of out-of-court administration appointments should be cogitated. There is the downside of out-of-court procedures though, which is the lack of accountability and transparency. Interviewee 3[192] had a similar concern:

> " … this could be a double-edged sword though with that profession as they may use it and abuse it more…Now yes, I think that if it wasn't going through court we would have seen more, now whether there would be an abuse of process though, I think that more people would try to take advantage of the legislation and the procedure… If you had in accordance with the legislation the obligation to go through the floating charge holder and giving them the option of

[191] Interviewee 5 (n 60).
[192] Interviewee 3 (n 59).

> appointing an individual of their choice then I think that would definitely be an improvement and it would lessen the chances of everything being opposed."

If out-of-court appointments are a perilous action, as the procedure will potentially be subject to manipulation, other hindrances must be overridden somehow. Examinership could only become the leading rescue procedure if receivership is ousted. If receivership is restricted, actions must be taken to amend examinership in a way that alternative options are provided to floating charge holders, since if this does not happen, they will be highly disenfranchised. The objections of creditors or shareholders against examinership[193] contribute to the delays thus, if the active role to appoint an IP was given to the floating charge holders, the process would be more sustainable. The DIP feature makes banks extensively cautious about the usage of examinership. Therefore, if enough control is given to the floating charge holders in examinership, the prospects of success could increase in comparison to the current circumstances.

In the light of Brexit, foreign companies might cease using the UK corporate rescue procedures. This could be devastating for the UK's economy and also people will lose their jobs due to the fact that it will be unnecessary to employ them for dealing with cross-border insolvencies. Companies from foreign jurisdictions that consider their available mechanisms non-compatible to their purposes, tend to prefer the UK procedures. Although there are some challenges, the UK insolvency processes are considered superior in comparison to the procedures of other countries thus, "forum shopping" is a frequent phenomenon in UK.[194] If the availability of administration is

[193] CAP. 113, Part IVA, s 202ΚΣΤ (1).
[194] John Wood, 'Cross-border Insolvencies After Brexit: Challenges and Recommendations' (2017) 5 NIBLeJ 7.

severely restricted post-Brexit, the most sensible outcome is that another jurisdiction will become the centre of insolvency.

It is legitimate for someone to think that it is just a small number of Cypriot companies that could benefit with a more attractive corporate rescue regime. The Cypriot insolvency procedures are recognised throughout the EU due to the Recast EU Insolvency Regulation 2015/848. This led to various arguments that the Cypriot regime could provide an appealing insolvency environment particularly in the EU.[195] To an extent, examinership is compatible with the 2019 directive since the required moratorium and a DIP feature are in place. However, a mechanism that facilitates rescue finance should be implemented to achieve harmony within the EU. Post-Brexit, if the rules are similar or identical to the UK rescue procedures, it is sensible that Cyprus could transform to the new centre of insolvency. Furthermore, given the fact that Cypriot procedures are less expensive than procedures in other countries, it could make the regime even more attractive. The development of Cypriot insolvency procedures is potentially depending on this. This could only be attained if the jurisdiction in Cyprus provides a reliable environment for companies to be persuaded to move their centre of main interests.

The above estimations might be too optimistic though, since as it is indicated above, examinership is barely considered by Cypriot companies due to several flaws of the procedure and features that are incompatible to the Cypriot reality. It is concluded that the applicability of examinership was not contemplated before its implementation. Examinership could be altered in a way that would be more similar to administration, which could potentially attract foreign companies for rescue and restructuring.

[195] Neocleous and Kyriacou, 'Explaining Cyprus's attractive restructuring regime' (n 8).

Chapter 6 – Selected Corporate Rescue Regimes

6.1 Introduction

While in previous chapters the standpoint of the United Kingdom (UK)[1] and Cyprus[2] towards corporate rescue was illustrated, a further element to the perception of rescue is derived through the consideration of the American and the Irish positions. Since various jurisdictions in Europe and internationally use Chapter 11 as a paradigm to their own rescue and restructuring mechanisms and it was also an example for the Directive (EU) 2019/1023 (the 2019 directive), its analysis is vital for answering the research question of this thesis.[3] The Cypriot examinership is modelled after the Irish examinership thus, the Irish approach could function as a lesson for Cyprus.

The United States of America (USA) has Chapter 11 as its leading restructuring mechanism. There has been a systematic criticism towards Chapter 11 in the USA since the initiation of the procedure through the US Bankruptcy Code (11 U.S. Code) in 1978.[4] This mechanism has particularly been described as "the pantheon of extraordinary laws that have shaped the American economy and society and then echoed throughout the world",[5] and thus it could not be absent from the analysis of this thesis. As the Cypriot examinership used the Irish examinership[6] as its archetypal model, this chapter explores the Irish examinership in comparison to the Cypriot examinership since the statistics suggest that the Irish examinership produces more

[1] See Chapter 2, 3 and 4.
[2] See Chapter 5 and Chapter 2 for a further perspective.
[3] Gerard McCormack 'Corporate restructuring law - a second chance for Europe?' (2017) 42 E.L. Rev. 532-561; Muir Hunter 'The nature and functions of a rescue culture' [1999] J.B.L. 520.
[4] Paul Lewis 'Change we can believe in? Chapter 11 and the American Bankruptcy Institute proposals for reform' (2015) 8 C.R. & I. 102-105.
[5] Elizabeth Warren, Jay Westbrook 'The Success of Chapter 11: A Challenge to the Critics' (2009) 107 Michigan Law Review 603, 604.
[6] Companies (Amendment) Act 1990 and now Companies Act 2014 (CA 2014).

efficient results.[7] Some of the arguments of this chapter are justified via drawing upon interviews that were conducted for this thesis.

The official term that is used in the USA is "bankruptcy" instead of "insolvency" but for the sake of consistency within this thesis the term insolvency will be used.[8] Both the USA Chapter 11 and the Irish examinership have a mutual aim, which is to save the company, while in both procedures there is a debtor-in-possession (DIP) feature. As such, Chapter 11 and examinership are the main reorganisation procedures in the USA and Ireland that are the equivalent of the UK administration. Administration and Chapter 11 are the paramount restructuring procedures in their continents as there has been a study that proved that both processes had excellent scores, especially after the various changes that were made on the procedures.[9] This chapter determines whether it would be compatible for the UK or Cyprus to mimic some of the Chapter 11 or the Irish examinership features, although the business and environment customs deviate in each country.[10]

Since Chapter 11 is one of the most prevalent and sophisticated restructuring mechanisms worldwide,[11] it is the main focus of this chapter. The Chapter 11 features that are scrutinised are the impact of DIP and the DIP financing agreements. The American attitude towards rescue is that it should be given as a right to all companies,[12]

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[7] Business in Ireland 2017 Annual Report <http://www.vision-net.ie/news/2017-annual-review-report> accessed 06 September 2019.
[8] The term bankruptcy is also used in the UK but only for personal insolvencies.
[9] John Townsend, 'Comparing UK and US business rescue procedures: are Administration and Chapter 11 perceived to be workable and affordable?' (2007) 23 IL and P 66.
[10] Gerard McCormack, 'Super-priority new financing and corporate rescue' [2007] J.B.L. 701-732.
[11] The USA ranks 2nd in the World Bank Doing Business Rankings on resolving insolvency. For these rankings see <https://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency/score> accessed 20 February 2020.
[12] This is connected to the creative destruction argument in which a discussion can be found in Chapter 2, Section 2.3.2.

which makes it different from the UK's approach[13] thus, an examination of the outcomes of Chapter 11 generates a further dimension to this thesis. There is a prime contrast between the viewpoint of the UK, which is regarded as creditor-oriented and the standpoint in the USA, which is viewed as debtor-oriented. Is the USA really debtor-oriented given the loose nature of its DIP and is the UK really creditor-oriented given the redistributive provisions and other provisions from the Enterprise Act 2002 (EA 2002)? This chapter explores whether the origins still hold true in practice by detecting the position of creditors and debtors in terms of control.

An interesting difference is that in Ireland, an examiner is also appointed while in the USA, an independent trustee is almost never involved. The Irish examinership attracted criticism during the early nineties, particularly from banks who believed that the legislation was against their interests as it was not providing satisfactory protection to them.[14] The First Report of the Company Law Review Group in 1994 suggested that the legislation should be amended in a way that the rights of creditors are not neglected.[15] The fact that examinership was not generating sufficient results led to the amendments of 1999 via the CA 1999 and the amendments of 2014 through the CA 2014. Even though the Irish examinership has gained more attention in the new millennium in comparison to the nineties, the number of companies that choose examinership is still discouraging. The Irish examinership was transplanted to the Cypriot insolvency regime but with some minor alterations that are clarified. This chapter indicates whether those differences produce any intended or unintended

[13] Sandra Frisby, 'In Search of a Rescue Regime: The Enterprise Act 2002' (2004) 67 M.L.R. 247-272, 248.
[14] First Report of the Company Law Review Group (December 1994) para 2.12.
[15] Ibid para 2.25.

outcomes. What is considered is *inter alia*, the statistical significance of the Irish examinership, the Irish legal background and the position of creditors.

6.2 Chapter 11 of the US Bankruptcy Code

6.2.1 Debtor-in-possession

The debtor manages Chapter 11 entirely[16] as there is not an administrator or an examiner analogous to the UK or Cypriot procedures respectively. The term DIP has been repeatedly mentioned throughout this thesis, but this chapter requires a more comprehensive investigation as it is a distinctive attribute of Chapter 11. The management displacement could cause both beneficial and unfavourable results and each jurisdiction has a discrete perception of it. Arguably, the fact that the management is not displaced in Chapter 11 is the characteristic that persuades the debtor to utilise it therefore, an analysis of the reasons is valuable.[17] Yet, the management might have not encountered issues of insolvency during their career thus, they might not be the most accountable and reliable people to deal with an insolvency case. It is sensible for one to expect that this will affect the outcome of Chapter 11 as to the number of company rescues in comparison to the main procedures of the UK and Cyprus. This leads to an explanation about the DIP operation and the influence on the major stakeholders.

The initiation of Chapter 11 is most commonly done voluntarily by the debtor company or it can be done involuntarily by the creditors of the company provided that particular criteria are satisfied.[18] The debtor has an active participation in Chapter 11 since s/he formulates the needed plan while continuing to manage as usual. Although it

[16] 11 U.S. Code § 1107.
[17] David Hahn 'Concentrated Ownership and Control of Corporate Reorganisations' (2004) 4 JCLS 117.
[18] 11 U.S. Code § 301, 303; Susan Block-Lieb, 'Why Creditors File So Few Involuntary Petitions and Why the Number Is Not Too Small' (1991) 57 Brooklyn Law Review 803.

has been argued consistently that it is the debtor that retains the powers regarding a reorganisation through Chapter 11, this plan can solely be inducted if the majority of creditors in number and if the two-thirds in amount of creditors in each class agree to it.[19] A stay[20] is triggered during Chapter 11 in which the debtor is further aided as the creditors cannot interrupt the procedure unless an objection is filed to the court.[21] Managers retain the right to take loans for the company or even use, realise and lease its assets in which court ratification is unnecessary.[22] The court's approval is imperative when the manager is acting outside the ordinary course of business of the company with the exclusion of using cash as security.[23] The secured creditor must be safeguarded by receiving 'adequate protection' therefore, court intervention is essential.[24] The court is further involved when it comes to Chapter 11 plans and the sale of substantial assets.[25] This a debtor driven procedure, with interference from external parties like the courts and creditors. The extent of the interference is challenged since Chapter 11 is criticised for the implied ample control that is given to creditors.

The debate on who should lead the restructuring process is rife in the USA and the UK. In the USA there is not a profession equivalent to the Insolvency Practitioner (IP) that the UK and Cyprus have, since such a person is not obliged to take the control of the company during restructuring.[26] The suitability of the manager retaining an extensive control over the ailing company is questionable. This is a contentious matter since English insolvency experts view this as inappropriate, but American insolvency

[19] 11 U.S. Code § 1126(c).
[20] 11 U.S. Code § 362; Term used for the moratorium in the USA.
[21] 11 U.S. Code § 362(m)(2)(A).
[22] 11 U.S. Code § 365(c)(2).
[23] 11 U.S. Code § 363; Lewis (n 4).
[24] 11 U.S. Code § 363.
[25] *Commodity Futures Trading Commission v. Weintraub* (1985) 471 US 343, 355.
[26] 11 U.S. Code § 1107.

experts are not treating the DIP feature in the same way.[27] Although this almost never happens, when a Chapter 11 case goes to court the judge evaluates the aptness of managers in handling the plan and if they are categorised as inadequate, they are replaced by a trustee.[28] Boundaries have been set concerning the dominance of the DIP still the courts are hesitating to perform that action.

As an IP is usually needed in regimes where the directors lose control, there are extensive direct costs because the fees of this profession are considerable. In Chapter 11 this kind of expense, where an independent trustee is not usually appointed, is avoided. Direct costs in this sense are curtailed but the involvement of the judiciary and lawyers do not make Chapter 11 a cheap process. Also, indirect costs such as a jurisdiction of unsuccessful rescues or the vitiation of a country's economy through the continued existence of insolvent companies, should be cogitated.[29] Interviewee 7[30] has the following opinion:

> " … I believe that lawyers and judges are not the right people to deal with insolvent companies, it is a business issue and it needs business people to be involved and frankly, involving a judge is an absolute waste of time in my opinion because judges don't know anything about these things. That is not what they are trained to do."

[27] Gabriel Moss, 'Chapter 11 - an English lawyers critique' (1998) 11 Insolv. Int. 17-20.
[28] David Skeel, 'Creditors' Ball: The "New" New Corporate Governance in Chapter 11' (2003) 152 University of Pennsylvania Law Review 917, 920.
[29] Rizwaan Mokal, 'Administrative Receivership and Administration—An Analysis' (2004) 57 Current Legal Problems 355-392, 366.
[30] Interviewee 7 (Lawyer/Academic) a law firm and a UK university (London, UK, 15 January 2019); see Appendix D.

This statement was an exaggeration since judges and lawyers who have experience in insolvency matters are capable of taking accountable decisions.[31] Arguably, an auditor is occupied by more financial knowledge and s/he probably has more experience in dealing with insolvent companies thus, s/he could produce more efficient decisions than a lawyer or a judge. What the interviewee is probably suggesting is that the financial knowledge of judges or lawyers is limited since the target of their training was not this, whereas accountants and auditors assess the soundness of a company maybe on a constant basis. The interviewee from the previous excerpt also had the following linking statement:

> "So, that may be expensive but it is also a sensible outcome. So, you then come to administration and you say: is that an expensive process? Well, yes, it is an expensive process but is it money well spent? If what you are doing is that you are spending money on insolvency accountants who are finding way to save the business I think that is money much better spent than paying judges and lawyers to argue over legal issues, which frankly have nothing to do with the saving of the business of the company."

The interviewee admits that administration is indeed a more expensive procedure since it is followed by various costs, but he is also suggesting that those expenses are worthwhile. His opinion is that this money is well spent because he considers accountants and auditors more competent in terms of rescuing the business than lawyers and judges. Nevertheless, the DIP can employ an insolvency expert that would help

[31] Vanessa Finch, 'Control and co-ordination in corporate rescue' (2005) 25 Legal Studies 374-403, 375.

him/her handle the reorganisation and/or appoint a new management. Statistics indicate that more than the 50 per cent of the USA managers are dismissed during the first two years of Chapter 11, while the figure during normal turnover is 6-10 per cent.[32] This demonstrates that when the manager cannot handle the situation s/he vacates the office but this is not always the case.

English scholars support the view that a major endogenous factor that contributes to company failure is mismanagement.[33] The perception and culture of a country is considered since in the USA for example, the management is not usually blamed for the adversity of the company.[34] Americans have more faith in the company management and it seems that they tend to assign the responsibility to the economy.[35] This is rather seen as a framework that minimises risk and encourages entrepreneurship. Finch suggests that the director is not the most appropriate person to undertake a rescue strategy since s/he already had the opportunity to turn over the company.[36]

Since the manager of the company might not be experienced in insolvencies – especially if the company is an SME – the expectation would typically be that s/he will undertake either biased or wrong decisions that can presumably harm the company and the other stakeholders.[37] However, the hands-on knowledge of the directors about the company makes them valuable players but this comes down to whether they should be in control.[38] A common impediment that would require the adept opinion of the director

[32] Vanessa Finch, David Milman, *Corporate insolvency law: perspectives and principles* (3rd edn, CUP 2017) 231; Kenneth Ayotte, Edward Morrison 'Creditor control and conflict in Chapter 11' (2009) 1 Journal of Legal Analysis 511-551, 522-523.
[33] Report of the Review Committee on Insolvency Law and Practice (Cmnd 8558, 1982) (Cork Report) 202-203; Kristin Van Zwieten, *Goode on Principles of Corporate Insolvency Law* (5th edn, Sweet & Maxwell 2019) 475.
[34] Moss, 'Chapter 11' (n 27).
[35] Bruce Carruthers, Terence Halliday, *Rescuing Business: The Making of Corporate Bankruptcy in England and the United States* (Clarendon Press 1998) 509-10.
[36] Vanessa Finch, 'Corporate rescue: who is interested?' [2012] J.B.L. 190-212, 203.
[37] Hahn (n 17) 127; Mokal (n 29) 366.
[38] Finch, 'Corporate rescue: Who is interested?' (n 36) 204.

is to determine the viability of company rehabilitation. When a company is at a terminal stage the director should go straight into liquidation without attempting to rescue the company as this could also harm the value of the remaining assets. This control is provided to the director as an incentive to pursue an early restructuring, because s/he will definitely not want to be removed. Therefore, if action is taken at the wrong time, the returns to creditors could be diminished.[39] The DIP feature has been unfair to creditors but there have been improvements since the initiation of Chapter 11 as creditors are in a far better position.

Early filing is encouraged when the management is left in place. This is the case for the USA at least since an insolvent company goes straight into liquidation. Liquidation happens through Chapter 7 of the US Bankruptcy Code, in which the management loses total control with an independent trustee being appointed. As a result, the DIP is wary about the timing of pursuing assistance from a mechanism, as the management is usually disgruntled when displaced. As previously mentioned, it is a major impediment when the directors file for a company voluntary arrangement (CVA)[40] or administration[41] when the company is already vastly deteriorated. Nevertheless, the chances of trading while insolvent in the UK are minimised by the wrongful trading provisions, in which there can be punitive consequences for the directors as they can be disqualified. However, the American regime rewards the management by keeping them in place, but a punishment that would restrict directors from possibly taking the wrong decisions and actions is absent. A federal law on restricting insolvent trading does not exist but there is a tort law equivalent.[42] This

[39] Hahn (n 17).
[40] See Chapter 3, Section 3.5.
[41] See Chapter 4, Section 4.2.1.
[42] *Schacht v. Brown* 711 F. 2d 1343 (CA Ill., 1983).

common law concept of "deepening insolvency" though covers more of a fraudulent trading situation rather than wrongful trading.[43] On a rare basis the judiciary takes into account the director's negligence that is akin to the wrongful trading in the UK.[44] It seems though that the application of deepening insolvency in negligent cases comes into conflict with the business judgment rule, which specifies that if the actions of the director happen in good faith s/he cannot be liable.[45] If the business judgment rule is bypassed at a constant basis though this could have a bearing on the incentives of directors who will be discouraged from pursuing the survival of the entity. This is likely to happen because directors would not want to jeopardise their position by being held personally liable. There could be a further consequence as there might be a hesitation to serve as corporate officer.[46]

In contrast to administration, Chapter 11 allows the cram down of secured creditors.[47] Hence, one could question whether Chapter 11 is debtor-oriented, as it has been consistently argued over the years. However, there might be a balance there due to the existence of the 'absolute priority rule' (APR). The rights of creditors are jeopardised though because there is a possibility of such directors to take actions that would diminish the value of their claims.[48] The most conventional means of devaluing

[43] Michael Schillig, '"Deepening insolvency" - liability for wrongful trading in the United States?' (2009) 30 Comp. Law. 298-303.
[44] *Smith v. Arthur Andersen LLP*, 421 F.3d 989, 1005 (9th Cir. 2005); *Gourian Holdings, Inc. v. DeSantis, Prinzi, Springer, Keifer & Shall (In re Gourian Holdings, Inc.)*, 165 B.R. 104, 107 (E.D.N.Y. 1994); Dmitry Konstantinov, 'Wrongful Trading: Comparative Approach (England and Wales, Russia and the USA)' (2015) 2 BRICS Law Journal 100-124.
[45] John Tully, 'Plumbing the Depths of Corporate Litigation: Reforming the Deepening Insolvency Theory' (2013) 2013 University of Illinois Law Review 2087, 2108; Daniel E Harell, 'Pandora's Bankruptcy Tort: The Potential for Circumvention of the Business Judgment Rule through the Tort Theory of Deepening Insolvency' (2005) 36 Cumb L Rev 151.
[46] Ibid.
[47] In the UK, cram down and a moratorium can take place at the same time if an administration and a scheme of arrangement are combined.
[48] David Skeel, 'Corporate Anatomy Lessons' (2004) 113 Yale Law Journal 1519.

the debt is the substitution of assets, the dismissal of claims and underinvestment.[49] Each case is different though thence, in certain situations creditors will not be at risk. In *LaSalle National Bank v. Perelman*[50] it was stated that: "[i]n the vicinity of insolvency, creditor interests gain a greater prominence though, as one court stated, the board of directors are not merely the agent of the residual risk bearers and are required to exercise informed good faith judgement so as to maximise the company's long-term wealth generating capacity." As creditors hold a crucial role in insolvencies, the court with this statement ensured that their rights will be safeguarded by promoting the good faith judgement.[51]

6.2.2 Who does Chapter 11 favour and how is this defining its rescue outcome?

6.2.2.1 Is Chapter 11 a pure pro-debtor procedure?

As Chapter 11 is in the control of the debtor it has invariably been argued that it is a pro-debtor process, but this is also a distortion of the connotation of this attribute.[52] Characteristics such as the DIP, the stay and the fact that there are no criteria to determine the insolvency of the company for using Chapter 11 have influenced this perception.[53] A misinterpreted aspect is the conveyed fairness of debtor-oriented and creditor-oriented approaches. Even though this section is focusing on Chapter 11, to ease the comparison between creditor and debtor focused approaches there are referrals to the UK administration, which has been depicted as a pro-creditor process.

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[49] Robert Rasmussen, 'The Ex Ante Effects of Bankruptcy Reform on Investment Incentives' (1994) 72 Washington University Law Quarterly 1159, 1168.
[50] (2000) 82 F Supp 2d 279 at 292–293; Gregory Varallo, Jesse Finkelstein, 'Fiduciary Obligations of Directors of the Financially Troubled Company' (1992) 48 Business Law 244.
[51] 11 U.S. Code § 1129 (a)(3).
[52] Gerard McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (EE Publishing 2008) 1.
[53] McCormack, 'Super-priority new financing and corporate rescue' (n 10) 702.

The main reason that the UK administration is considered as pro-creditor is because the debtor is replaced with an IP, which has been described as a hard approach towards the management.[54] This comes into conflict with the fact that during administration, a moratorium is triggered, which creditors can reflect as a prejudice. Scholars support that after the EA 2002, the UK administration has taken a move towards debtors in which a balance has been created between stakeholders.[55] Rajak was confident enough to suggest that "we may yet see the most dynamic insolvency regime in the world".[56] He said this because, through the EA 2002, rescue is facilitated although it is not compulsory to have such an outcome.[57]

In every insolvency there is always one stakeholder that is harmed more than another, but the satisfaction of all the involved parties is implausible. If a jurisdiction takes an utmost side either towards debtors or creditors it would mean that not much attention is given to other stakeholders therefore, many creditors could be vitiated. That said, if a middle ground is detected, a minority of stakeholders will be harmed and the conveyance of impartiality will materialise. Nonetheless, Kilpi argues that a debtor-oriented regime is aligned with utilitarianism ethics because it decreases the detriment to the society and that it is irrational to ask from the debtor an amount that would be essential to its sustainability.[58] Maybe this scholar is suggesting this because through rescuing the company, a corporate debtor could save jobs and prevent other creditors from precipitating insolvency. These outcomes could provide some wider economic benefit that amongst other things include no redundancy payments by the state, preserving tax flow to the state and no job seekers allowance paid by the state. Despite

[54] Sefa Franken, 'Creditor- and debtor-oriented corporate bankruptcy regimes revisited' (2004) 5 E.B.O.R. 645-676.
[55] Harry Rajak, 'The Enterprise Act and insolvency law reform' (2003) 24 Comp. Law. 3.
[56] Ibid.
[57] See Chapter 2 and Chapter 4.
[58] Jukka Kilpi, *The Ethics of Bankruptcy* (Routledge 1998) 70.

that, Chapter 2 of this thesis illustrates that there are some instances where the sale of assets could be advantageous to the majority of stakeholders rather than having a meaningless rehabilitation that could possibly collapse within a year. A utilitarianism approach is followed when there is a balance in the interests of stakeholders even if that means that a minority is disadvantaged. Therefore, this outcome could be present in either a debtor or a creditor favouritism regime.

A clarification on whether a jurisdiction follows a creditor-oriented or a debtor-oriented approach is crucial since it is sensible that the perception towards rescue is different as well as the incentives. There is proof that an orientation towards creditors or debtors signifies the contingency of saving an entity. A pro-debtor mechanism certainly encourages company rescue more than a pro-creditor process. Yet, this does not mean that in Chapter 11, that is categorised as pro-debtor, the rehabilitation of an enterprise will happen in all junctures. The fact that in a DIP process the debtor has the control of negotiations, suggests that company rescue is more conventional outcome in a debtor-oriented process.[59] The result cannot be predictable in certain occasions though. McCormack says that in Chapter 11 there is not a substantial motive to increase the prospect of company rehabilitation but to secure better claims for creditors.[60] When the centre of interest of the process is exclusively on creditors, the priority would be to increase value of assets to secure more returns for them therefore, the expectancy of saving an entity is minimal. However, if circumstances on whether there is a clear orientation are vague, a strenuous assessment as regards the outcome of the procedure is created.

[59] Ron W. Harmer, 'Comparison of Trends In National Law: The Pacific Rim' (1997) 23 Brook.J.Int'lL.146, 147-148.
[60] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 150-151; The end of bankruptcy

During the first years of Chapter 11 debtors were in immense dominance. Their pre-eminence was conspicuous to the extent that they were exploiting the investments of creditors.[61] Chapter 11 cases had an ample duration therefore, money that were supposed to be available to creditors were exhausted in an attempt to a trivial rescue of a company. The current situation in the USA – that is potentially generating impediments – is that there is too much prejudice towards saving companies. A plethora of emphasis is rendered on enterprises that should have been liquidated in the first place.[62] A paradigmatic example is the bankruptcy of Eastern Airlines that occurred in the late 80s. There were signs that Eastern Airlines should have been sold when the struggle started. The CEO of the Eastern Airlines deferred any action that could put the enterprise into a better position, which caused the diminution of its value and as a result the company assets were realised at a downgraded price. This outcome attracted much criticism, where the censurers were requesting amendments to occur. There were several debates in which the accountability of Chapter 11 was questioned and also an evaluation on whether this process should be substituted by a mechanism that is more market-oriented.[63] A common understanding was potentially engendered, since while there was ignorance as regards discipline within the market, things took another turn. This was the natural evolution of the issue since this change took place without any amendments to the legislation.

[61] Lynn LoPucki, 'The Trouble with Chapter 11' (1993) 3 Wisconsin Law Review 729, 739-745 about the duration of cases.
[62] Daniel Altman, 'Chapter 11? Or Time to Close the Books?' N.Y. TIMES, 15 December 2002 <https://www.nytimes.com/2002/12/15/business/chapter-11-or-time-to-close-the-books.html> accessed 24 August 2019.
[63] Barry Adler, 'Financial and Political Theories of American Corporate Bankruptcy' (1993) 45 Stanford Law Review, 311, 323-333; Douglas G. Baird, 'The Uneasy Case for Corporate Reorganizations' (1986) 15 The Journal of Legal Studies 127, 136-38.

Ayotte and Morrison suggest that: "Chapter 11 does not provide a safe harbor for entrenched managers."[64] Conceivably, they say that this is due to the rights that creditors have gained since the enactment of the Bankruptcy Code. A mechanism that was once criticised for exploiting creditors and for being extensively focused on debtors is now said to be an ominous place for managers. This comes into conflict with the deliberation about the debtor-oriented perception of Chapter 11. Recent changes have been more intense as regards to the dominance of Chapter 11. Creditors used to be in the vulnerable cast but now they seem unsusceptible due to the various protections that they are currently enjoying. A USA reorganisation plan can only be granted by the courts if all the denominated voting classes of creditors provide their consent.[65] If a dissenting class of creditors disagrees with the plan that was formed by the DIP, the dissenting creditors can be crammed down only if the plan produces fair and equitable results to them. The creditors that object to the plan will be guarded by the 'best interests' test where they should receive a higher amount than they would have received in liquidation.[66] The 'feasibility test' is also essential because it signifies the viability of the promises of the debtor within the plan.[67] There can be an agreement, *inter alia*, to assure them that the dissenting class is going to be fully paid or that any creditor class that ranks below them will not acquire any returns.[68] This shows that even in occasions where creditors are crammed down, the legislation restores the fairness with other rules.[69] These rules however, exemplify that although Chapter 11 provides the impression that it is the debtor who gains in this procedure, in reality creditors are not

[64] Ayotte and Morrison (n 32).
[65] 11 U.S. Code § 1128(a).
[66] Gerard McCormack, 'Control and corporate rescue - an Anglo-American evaluation' (2007) 56 I.C.L.Q. 515-551, 518.
[67] Ibid.
[68] 11 U.S. Code § 1129(b)(1).
[69] Franken (n 54) 651.

treated unjustly. Friedman also added that: "the traditional mystique concerning cram down which instils fear among secured creditors is exaggerated."[70] He also highlights that cram down is done in uniform and foreseeable modus when secured creditor claims are considered.

Chapter 11 was once exploited by managers as an anti-takeover mechanism, no longer has that use. Now there has been an orientation towards the market, the returns to creditors are maximised and it facilitates asset sales and cases end quicker.[71] While in the 1980s creditors seemed to be the disadvantaged players of reorganisations, today they are not overshadowed by managers who used to maintain a central role. What caused this was the distressed-debt trading and the DIP financing agreements.[72] Distressed-debt trading can be correlated to globalisation and the evolvement of financial markets. A supplier sells the debt that is owed to him/her thus, this could mean that the new debt holders might not be interested in keeping a good relationship with a company that they previously did not have any interactions with. Ostensibly, these debt holders will probably not be interested in maintaining the soundness of the company.[73] These traders are commonly hedge funds that hesitate to venture their fund in order to aid with the recovery of the entity. An analysis on the control of creditors during DIP agreements is analysed below in section 6.2.3 since the power of creditors is enhanced with such agreements.[74]

Various rights were retrieved from creditors in the USA, but this does not mean that the courts are not favouring debtors. The public and courts do not empathise with

[70] Jack Friedman, 'What Courts Do to Secured Creditors in Chapter 11 Cram Down' (1992) 14 Cardozo Law Review, 1495.
[71] Skeel, 'Creditors' Ball' (n 28) 921; McCormack, 'Control and corporate rescue - an Anglo-American evaluation' (n 66).
[72] Harvey Miller, Shai Waisman, "Is Chapter 11 Bankrupt" (2005) 47 Boston College Law Review 129, 152.
[73] Ibid.
[74] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 46.

creditors as there is the conception that they are afflicting the company debtors.[75] There is also a tendency of preference towards risk takers and not banks or financiers, which is totally different from the UK and Cypriot attitude. Chapter 11 that was criticised in the past for allowing an extensive control from debtors, is now shifting towards creditor control. Chapter 11 did not yet enter the pro-creditor cluster since as per the international standards is deemed as pro-debtor.[76] This happens because managers are still in place thus, they have more control than in a process from which they are completely displaced and cannot influence any of the decisions. Contrariwise, Skeel suggests that: "[a]though bankruptcy law does not formally authorize creditors to displace the company's directors, creditors have increasingly exercised de facto control."[77] Creditors impart threats to directors that they should resign because they will eventually be replaced regardless.[78] The creditors can bring a chief restructuring officer to the picture, who along with the debtor creates the required plan. This is notably denoting that the creditors can affect the selection of these officers by providing a list of candidates or by giving an approving or a disapproving response to their selection.[79] According to McCormack "[t]he Enterprise Act has made some modest moves down the Chapter 11 path but Chapter 11 practice has itself moved in a more market-led direction.[80]" Although a procedure could be classified as being pro-creditor or pro-debtor this does not signify that either orientation will not be effective.

[75] Moss, 'Chapter 11' (n 27).
[76] Skeel, 'Creditors' Ball' (n 28) 921.
[77] Ibid 922.
[78] Jared Sandberg, Joann Lublin, 'Who Runs WorldCom?' 26 June 2002, The Wall Street Journal <https://www.wsj.com/articles/SB1025044139757626480> accessed 27 August 2019.
[79] Douglas Baird, 'The New Face of Chapter 11' (2004) 12 American Bankruptcy Institute Law Review 69.
[80] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 306.

6.2.2.2 The attitude of the US towards company rescue in comparison to the UK

In Chapter 11 there is no need of the company being insolvent either on balance sheet or equity basis.[81] Arguably, Chapter 11 can be used as stratagem but the good faith requirement limits the extent of misuse.[82] Even though there is not a particular criterion, the intention of restructuring or liquidating or selling the business should be present.[83] As discussed in *Re SGL Carbon Corporation*[84]if the purpose of the plan is not sincere, its dismissal will be inevitable. This clarification is important since if the company was liquidated instead of undertaking a rescue attempt, the value of it would have been reduced which would have left the creditors exposed. That said, although the perception is that all actions that could rehabilitate the company should be exhausted, the various functions of Chapter 11 does not make it *de rigueur* to save the entity.

The USA, the UK and Cyprus are all being committed to rescue culture, where the legislators of these countries attempted to replicate it in a way that would have been aligned with their jurisdiction. Sensibly, each country discerns the notion of rescue from another angle. In the UK insolvencies are considered as serious embarrassments[85] and that not all companies should have the option of rehabilitating. Many Americans now consider insolvency a rite of passage in commercial life.[86] With the implementation of Chapter 11, the Congress contemplated that the allowance of company reorganisation would combine the maintenance of jobs, returns that would indulge creditors and ensure that the owners are not left with nothing. It is in all situations more beneficial to at least save the business rather than sell the company assets as a piecemeal.[87] The

[81] Finch and Milman (n 32) 236.
[82] Ibid.
[83] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 79.
[84] (1999) 200 F3d 154.
[85] Nathalie Martin 'Common-Law Bankruptcy Systems: Similarities and Differences' (2003) 11 American Bankruptcy Institute Law Review 367, 374.
[86] See further discussion about this in Chapter 2, Section 2.3.1.
[87] *US v. Whiting Pools Inc* (1983) 462 US 198, 203.

circumstances in the UK depart from this since failing businesses tend to continue to carry the stigma of once being insolvent.[88] The opportunity of saving the company and/or business even though it is encouraged is not available to all companies.[89] If in the UK, the option of rescue was given to all companies, it could have been paralleled to the fuelling of a deteriorated economy.[90] Through the EA 2002 there was an attempt to countenance entrepreneurship and minimise the risk of ailing companies with the aim of enhancing the UK economy. However, there is a long way until administration is classified as a process that mainly pursues company rescue, which is arguably never going to happen.

When interviewee 8[91] was asked whether the UK procedures should turn into more rescue-oriented instead of having the debt collection as a core aim, he answered the following:

> "In Chapter 11 they probably do it more successfully than anyone else but a lot of the powers that they have in Chapter 11, that the judges have or the companies have to apply tend to be very anti-creditor and very debtor-friendly…So they could do lots of very progressive things in restructuring and there is less kind of public outcry about it and less creditor outcry because the judge stamps it and we are a million miles away from that."

As the Chapter 11 plan goes before a judge who has to approve it, creditors are probably not filled with indignation since it binds all stakeholders. This interviewee believes that

[88] Martin (n 85)
[89] Sandra Frisby, 'In Search of a Rescue Regime: The Enterprise Act 2002' (2004) 67 M.L.R. 247-272, 248.
[90] Moss, 'Chapter 11' (n 27).
[91] Interviewee 8 (Insolvency Practitioner) Big Four (London, UK, 19 January 2019); see Appendix D.

Chapter 11 favours the debtor into the extent that it facilitates a more rescue-oriented mechanism and the fact that the plan is sanctioned by the judge, it provides less criticism and public outcry that eases the procedure. In accordance to the interviewee's statements, in the USA there is structured system in which the path to company rehabilitation is easier than in the UK. Statistics on the outcome of both Chapter 11 and administration are imperative as with this comparison, the comprehension of whether business rescue should be seen negatively is stipulated.[92]

Debtor replacement mechanisms have an inclination towards accomplishing business rescue instead of the rehabilitation of a company. Business rescue though includes the preservation of employment and it restricts the negative impact on suppliers. This is what happens in the UK administration, but with the EA 2002 steps were taken towards actively encouraging company rescue. Even though these actions were taken, company rescue is still regarded as a vast threshold that is difficult to override. Martin says that: "It is not, however, a reorganisation in the traditional American sense of the word."[93] Albeit steps were taken towards a path of rescue, this is still not the American standpoint. The only real rescue from their viewpoint is if the company shell along with the business are saved.[94] When cogitating traditional concepts though, there should be an appraisal on whether this deviates from reality.

Baird and Rasmussen put forward the thesis that: "[c]orporate reorganizations have all but disappeared."[95] Rescue other than the company rescue is not considered a success in the USA,[96] but the aforementioned quotation suggests that even though this

[92] The results of the UK statistics are part of the empirical research of this thesis, but for the American statistics, sources that tested empirically the outcome of Chapter 11 will be used.
[93] Martin (n 85) 397.
[94] Van Zwieten (n 33) 479-480.
[95] Douglas Baird, Robert Rasmussen, 'The end of bankruptcy' (2002) 55 Stanford Law Review 751-789; Supported by the judiciary: *In re Chrysler LLC*, 576 F.3d 108, 115 (2d Cir. 2009) and *In re Gulf Coast Oil Corp.*, 404 B.R. 407, 418–19 (Bankr. S.D. Tex. 2009).
[96] See Chapter 2, Section 2.3.

could be the perception, the pragmatism is not as anticipated. This proclivity necessitates a comparison with the relevant statistics to view the correspondence with this connotation. Currently, Chapter 11 can also function as a device that divides and sells company assets.[97]

The epilogue of a case is decisive for a practitioner/debtor that handles an insolvency process as it could designate his/her tactic.[98] In a Chapter 11 plan, the likely legal outcomes are the following: a number of cases are dismissed by the courts,[99] others are transmuted to Chapter 7 cases instead in which trading ceases and the assets are liquidated for the advantage of creditors,[100] and the last is the approval of the reorganisation plan.[101] Statistics show that while the confirmation rate of the court was once at 11 per cent it evolved to 30-33 per cent but after a 10 year analysis the rate reaches the 45 per cent although some reservations about this have been provided.[102] The economic outcomes of the approved plan must also be assessed as they do not always end up in rescue. According to an empirical study about companies that used Chapter 11 during 1997-2004, the following outcomes arose: 36.7 per cent were rescued through the reorganisation of the company, 42.2 per cent sold the whole or part of their business and 21.1 per cent were liquidated with the assets being sold as a piecemeal.[103] A reservation about the statistical significance of this study is accentuated since the sample consisted of a small number of 90 companies. There is another empirical study

[97] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 306; Stephen Lubben, *American Business Bankruptcy: A Primer* (EE Publishing 2019) 96.
[98] Warren Agin, Gill Eapen, 'Predicting Chapter 11 Bankruptcy Case Outcomes Using the Federal Judicial Center IDB and Ensemble Artificial Intelligence' (2019) 35 Georgia State University Law Review 1093-1115.
[99] 11 U.S. Code § 1112.
[100] 11 U.S. Code § 701–84.
[101] About the confirmation rates of reorganisation see Warren and Westbrook (n 5) 615 and Greg McGlaun, 'Lender Control in Chapter 11: Empirical Evidence' (February 2007) 521 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=961365> accessed 26 August 2019.
[102] Ibid.
[103] McGlaun (n 101).

on Chapter 11 that only considered large firms, which had contiguous numbers as regards to company reorganisations since it reached the 32 per cent.[104] The slight difference in the numbers is probably because large corporations pursue a pre-packaged Chapter 11.[105] Since the investments of creditors exceed the funds that are invested by creditors of small companies, there is usually pressure to have a quick sale to avoid value deterioration.[106] This kind of sale is a method to avoid a long-lasting procedure, as it makes sure that the value of the assets will not drop and ensures the feasibility of selling the assets at the highest price.[107] Therefore, it seems that Chapter 11 also took a form of addressing issues concerning mergers and acquisitions.[108]

Even though the percentage of rehabilitation in the USA is not as expected, it is still better than administration that only reaches the 0.5 per cent.[109] This is evidence that the argumentation that there are higher probabilities of saving the entity in the USA is valid. The business sale percentage is still lower than in the USA since according to the quantitative data analysis of this research about the UK administration, the percentage is at 34.9 per cent. While the most common result of administration is the sale of assets that reaches the 64.6 per cent, in the USA this is the less likely outcome. Scholars argue that this is owed to the DIP feature but also to the financing mechanism that is expedited through Chapter 11.[110]

Subject to Insolvency Act (IA 1986), Sch B1, para 73, in the UK secured or preferential creditors cannot be crammed down. However, the analogous Chapter 11 cram down can be enabled through twinning administration with schemes of

[104] Ayotte and Morrison (n 32) 521.
[105] On pre-packaged sale: 11 U.S. Code § 363(b); For a discussion on the UK pre-packs see Chapter 4, Section 4.5.
[106] Ayotte and Morrison (n 32).
[107] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 286.
[108] Douglas Baird, *Elements of Bankruptcy* (4th edn, Foundation Press 2006) 232.
[109] For more information see Chapter 2, Section 2.4.1, Graph D.
[110] McGlaun (n 101).

arrangement. This enables a moratorium and at the same time generates a cram down to junior creditor classes, but the combination of these procedures can be burdensome and expensive.[111] A cram down mechanism could potentially encourage rescue, which corresponds with the government's opinion who stated that it: "would be a useful addition to the UK's business rescue tools".[112] This device could also ease the procedure and accelerate rescue since it would oblige resisting creditors to cooperate.[113] If this addition comes into effect in the UK, it could promote consensual restructurings and as argued by the government, the status of the UK as "a leading global restructuring hub" could be preserved.[114]

The fact that Chapter 11 is classified as pro-debtor does not necessarily denote that this is what impacts the rise of company rescues, but other features such as DIP financing are prominently conducing to this. The anticipation in the UK is not tantamount since it is more contingent to have a business rescue or the realisation of assets instead of company rescue.[115] Through observing the statistics, Chapter 11 is a far better procedure than administration. Administration is considered one of leading and most respectful rescue procedures worldwide though.[116] It seems that Chapter 11 is more effective in terms of rescuing the entity, but other obstacles might be generated that could be a burden to several stakeholders. McBride questions whether "the U.S.

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[111] Jennifer Payne, 'Debt Restructuring in the UK' (2018) 15 European Company and Financial Law Review 449-471, 465.
[112] Department for Business, Energy & Industrial Strategy, Insolvency and Corporate Governance – Government Response (26 August 2018) (ICG Report 2018) 5.148, 5.163.
[113] Sandra Frisby, 'Of rights and rescue: a curious confluence?' (2019) Journal of Corporate Law Studies <https://www.tandfonline.com/doi/pdf/10.1080/14735970.2019.1615165?casa_token=6utFTENN-j8AAAAA:6Rfb7XRQ3-1G3boYCP-A6lxraRtFLFdzpaPWI1X2RL9cvOBLaLMgaVBiuddu9nMj8Bhk4DNcBqRL> accessed 17 December 2019; McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 88.
[114] ICG Report 2018 (n 112) 5.148.
[115] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 116, 307.
[116] The UK ranks 14th worldwide in the World Bank Doing Business Rankings on resolving insolvency. See <https://www.doingbusiness.org/en/data/exploretopics/resolving-insolvency/score> accessed 21 February 2020.

system – one that follows a 'rescue' approach... – wastes economic resources, diverts funds to hefty legal and consulting fees and slows down overall economic growth".[117] In the USA there is the perception that all available resources for achieving company rescue should be exhausted. This happens even in occasions where the probabilities of having a successful rescue are limited.

6.2.3 DIP financing and the control of creditors

Securing finance during rescue is indispensable for the company to have a prospect of being kept sound.[118] If the company does not secure a source of funding, a rescue mechanism cannot be used for its chief purpose, which will have as a result the realisation of assets on a piecemeal basis and the ultimate option would be to wind up the entity.[119] Before the enforcement of Chapter 11 to the Bankruptcy Code, these agreements were called a receiver's certificate.[120] The DIP financing agreements have grown to be of primary significance for Chapter 11 plans, as these agreements now function as a governance device.[121] The use of Chapter 11 with the absence of a financing agreement can cause various reverberations. For instance, valuable time is wasted in the search for funding as the company will be in need of urgent cash-flow. Even though the existence of financing agreements is pivotal for the successfulness of Chapter 11, it could also provoke some detriments.

That said, motivations must be provided to existing or new creditors that would persuade them to provide a cash injection to ailing companies. New creditors hesitate

[117] Sarah McBride, 'Australia's Tough-Minded Bankruptcies May Serve as Role Model' (2002) Wall Street Journal A2.
[118] See Chapter 4, Section 4.7.
[119] McCormack, 'Super-priority new financing and corporate rescue' (n 10).
[120] David Skeel 'The Past, Present and Future of Debtor-in-Possession Financing' (2004) 25 Cardozo Law Review 1905.
[121] Governed by 11 U.S. Code § 364.

to lend money since there might not be anything left for them if the company goes bust.[122] Also, there might be a security over all assets of the companies thus, current creditors might be unwilling to expand their exposure. This could happen although a DIP cannot enter into security agreements without court approval. If the existing creditors do not have enough incentives though, they might cease the finance that they were previously providing to the company. Debtors search for new creditors on a rare basis, since it is the pre-petition creditors who are more aware about the finances of a company and at the same time § 364 of the 11 U.S. Code creates an infrastructure of protections, that is persuading these creditors to fund the procedure.[123]

The system of financing in Chapter 11 is allowing super-priority to creditors that provided rescue finance, but the fortune of other creditors is precarious.[124] If the company is eventually liquidated after Chapter 11, any debts that were incurred after the restructuring plan was passed are prioritised over the claims of unsecured creditors that took place prior to the petition.[125] This occurs automatically if this raising of funds is within the usual course of business. Otherwise, the judge will have to sanction the priority before the credit is authorised.[126] There are also some protections that encourage creditors to fund the debtor company even after the petition has been made.[127] For instance, it is predominantly the DIP who determines whether executory contracts will be assumed or rejected, but the DIP is not allowed to assume a contract with a purpose of receiving a loan or to get additional finance when rescue finance has been secured.

[122] George Triantis, 'A Theory of the Regulation of Debtor-in-Possession Financing' (1993) 46 Vand. L. Rev. 901.
[123] Sandeep Dahiya et al., 'Debtor-in-Possession Financing and Bankruptcy Resolution: Empirical Evidence' (2003) 69 Journal of Financial Economics 259; McGlaun (n 101).
[124] This is the effect of IA 1986, Sch B1, para 99 that prioritises administration expenses. See details in Chapter 4, Section 4.7.
[125] 11 U.S. Code § 364.
[126] McCormack, 'Super-priority new financing and corporate rescue' (n 10).
[127] 11 U.S. Code § 365(c)(2).

The courts ordinarily do not permit a restructuring plan if the credit is not transferred to the company in advance. In occasions where a financing agreement is not formed, a Chapter 11 plan can only be authorised if the new creditor is guaranteed the full return of his/her credit.[128] Financing could be accelerated through debt-purchase agreements like invoice agreements. Supply on credit terms from trade creditors is crucial hence, financing agreements operate as an advantage for trading reorganisations. This occurs because if the credit suppliers are prioritised, they will probably be more willing to cooperate.

A substantial difference between the stay through Chapter 11 and the moratorium through administration is that in the USA the stay forbids suppliers and customers from putting an end to their contracts if the factor of this decision arises from insolvency issues. While this happens in the USA, in the UK these stakeholders can terminate their contracts, solely on insolvency grounds.[129] The analogous *ipso facto* prohibition clauses that are in effect in the USA cannot be triggered in the UK due to the conflict with the anti-deprivation rule.[130] This argument was reinforced by *Belmont Park Investments PTY Limited (Respondent) v. BNY Corporate Trustee Services Limited and Lehman Brothers Special Financing Inc*[131] where it was stated that the influence of the anti-deprivation principle was overriding to the extent that it could not be set aside. The termination of contracts, however, makes it impossible to attract new financing and therefore continue the trading of the company while in a rescue

[128] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 184.
[129] Jennifer Payne, 'Debt Restructuring in English law: lessons from the United States and the need for reform' (2014) 130 LQR 282; Payne, 'Debt Restructuring in the UK' (n 111).
[130] Felicity Toube, Joanne Rumley 'A brave new world? Should the UK ban ipso facto clauses in non-executory contracts?' (2018) 31 Insolv. Int. 78-83; Gabriel Moss, 'Anti-deprivation, flip clauses, ipso facto rules and the Dante inferno' (2017) 30 Insolv. Int. 24-27.
[131] [2011] UKSC 38.

process.[132] When interviewee 1,[133] was asked to provide his opinion about super-priority he replied the following:

> "I think that would be a positive step for restructuring since the suppliers will continue to trade on credit during that period, if you pass them super-priority. I mean it would not cover their old debt but at least it would cover their current trading. I think that institutions like banks would be against it because they would see it as diluting their priority… I think that super-priority might be seen negatively by banks and by financial institutions."

The main reason that there is a hesitation of implementing this characteristic in the UK is owing to the forecasted opposing reaction of creditors, who probably feel that they have been deprived of their rights. The provisions that are included in the directive on preventive restructuring frameworks that was implemented in June 2019 are the closest version to Chapter 11 DIP financing provisions.[134] Even though calls have been made for DIP financing provisions to be adopted at a European level,[135] the Directive makes reference to priority rules, but there is nothing equivalent to the super-priority provision of the 11 U.S. Code.[136] Yet, EU member states will have the resilience to enforce these rules in accordance to the needs of the country's legislative culture, which means that

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[132] Ben Larkin et al., 'Restructuring Through US Chapter 11 and UK Prepack Administration' in Christopher Mallon and Shai Waisman (ed.), *The Law and Practice of Restructuring in the UK and US* (OUP 2011) 214.
[133] Interviewee 1 (Credit Manager) (By phone, UK, 04 December 2018); see Appendix D.
[134] The 2019 Directive, Article 17.
[135] Association of Financial Markets in Europe (AFME)/Frontier Economics, 'Potential economic gains from reforming insolvency law in Europe' (February 2016) 18 <https://www.afme.eu/Portals/0/globalassets/downloads/publications/afme-insolvency-reform-report-2016-english.pdf> accessed 22 September 2019.
[136] Jennifer Payne, Janis Sarra, 'Tripping the Light Fantastic: A comparative analysis of the European Commission's proposals for new and interim financing of insolvent businesses ' (2018) International Insolvency Review 178.

some member states might go even further and adopt rules that are akin to the super-priority provisions in the USA. Hence, this could have a different impact on each EU member state that could also come into contrast with the input of the Chapter 11 DIP financing. Cyprus will have to implement a financing device that would be available to financially struggling companies although banks might be against this. Through the years, there have been recommendations about implementing such a device in the UK, with the latest being in August 2018 through a government consultation.[137] Therefore, post- Brexit, the UK might decide to enforce the financing agreement provisions that would allow super-priority therefore, the UK insolvency regime will be harmonised with the regimes of other EU member states.

The formation of financing agreements have advantageous outcomes for both debtors and creditors, yet sometimes such agreements are not suitable.[138] There has been a steady rise in these agreements but the maximum that has been recorded is 48.21 per cent.[139] This empirical research took place more than fifteen years ago hence, maybe the case today is distinct as the value of DIP financing is of ample magnitude for the entity due to its rescue prospect. It is usually the debtors of large companies that pursue financing agreements, which means that it is more feasible for large companies to utilise and have an effective Chapter 11 result.

Creditors tend to enhance their position due to the neediness of debtors for immediate cash injection through the implied authority the legislation has provided to them. The creditor might set a requirement of employing a chief restructuring officer to make investigations and eventually suggestions on the plan that the debtor is supposed

[137] ICG Report 2018 (n 112).
[138] Skeel 'The Past, Present and Future of Debtor-in-Possession Financing' (n 120).
[139]Dahiya et al. (n 123).

to create.[140] The loan can contain several constraints about the utility of the company funds that the creditor provided.[141] The establishment of a fine relationship between debtors and DIP creditors is of eminent importance, which means that debtors will probably accept the requirements of creditors.

A crucial part of the loan agreements is the inclusion of affirmative and negative covenants. With a strategy by DIP creditors, notably negative covenants have the ability of augmenting their control over the company. An empirical study discovered that, 9 out of 10 companies that utilised a DIP loan in Chapter 11 have limitations as regards their activities and expenses.[142] Various problems are engendered by the use of these covenants though. For instance, if arduous deadlines are contained within the agreement it could bring the company into a deadlock as it could force the liquidation of the company, where the entity would be deprived the possibility of being saved.[143]

The compelling interest of creditors to preserve the value of the company makes a financing agreement beneficial. This means that various risk averting provisions have been included by these creditors into the agreements. This forces the debtor to not take any precipitous or jeopardising decisions concerning the business tactics of the entity.[144] These limitations are keeping the financial state of the company steady, but if it means that liquidation would be more advantageous for the creditor there would be pressure for that to be done. The prevention of risk could come into conflict with an investment that could possibly maximise the value of the business and assets. The company is not be allowed to make such investments as the value could be suddenly reduced. If the

[140] Douglas Baird, Robert Rasmussen, 'Four (or Five) Easy Lessons from Enron' (2002) 55 Vand L Rev 1787, 1807.
[141] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 188.
[142] Sris Chatterjee et al., 'Debtor-in-Possession Financing' (2004) 28 Journal of Banking & Finance 3097–3111, 3108.
[143] Barry Adler, 'Bankruptcy Primitives' (2004) 12 American Bankruptcy Institute Law Review 219, 222.
[144] Skeel 'The Past, Present and Future of Debtor-in-Possession Financing' (n 120) 1907.

investment had occurred and succeeded though, this would mean that confidence is created towards saving the company. However, even though it is not viable for Chapter 11 cases to function without DIP financing, it is one of the reasons that company rescues cannot go beyond 36.7 per cent.[145]

Another aspect of DIP financing that gives rise to criticism is that pre-petition creditors can leverage their position as regards to their old loan though "roll-ups" or cross-collateralisation by becoming the DIP creditors.[146] A "roll-up" is practically ensuring the full repayment of the old loan, which rolls up into the new loan. With "cross-collateralisation" an encumbrance will be attached on the unsecured creditors of the company since the DIP creditor will probably demand prioritisation. This generates impediments but the positive facet for the debtor is that an existing creditor might provide financing on better terms than a new creditor.[147] This issue can be tackled if the courts do not pass an order that would protect loans that were formed before Chapter 11. Skeel notes that this could be done by dealing with pre-petition and post-petitions loans distinctly and by particularly ensuring that the pre-petition loans will rank lower than post-petition loans.[148] Finally, another suggestion would be to provide the existing creditors the "right of first refusal".[149]

[145] McGlaun (n 101).
[146] Charles Tabb, 'A Critical Reappraisal of Cross-Collateralization in Bankruptcy' (1986) 60 S Cal. L. Rev. 109.
[147] McCormack, 'Super-priority new financing and corporate rescue' (n 10); James White, 'Death and Resurrection of Secured Credit' (2004) 12 American Bankruptcy Institute Law Review 139, 169.
[148] Skeel 'The Past, Present and Future of Debtor-in-Possession Financing' (n 120).
[149] Sarah Paterson, 'The Insolvency Consequences of the Abolition of the Fixed/Floating Charge Distinction' (January 2017) Secured Transactions Law Reform Project Discussion series, 15; Sofia Ellina, 'Administration and CVA in corporate insolvency law: pursuing the optimum outcome' (2019) 30 I.C.C.L.R. 180-191, 190; See also Chapter 4, Section 4.7.

6.3 Examinership in Ireland

6.3.1 Is the Irish examinership successful in comparison to the Cypriot examinership?

Examinership was introduced into Ireland with the purpose of enabling the corporate rescue option to companies, in response to an economic crisis in the beef industry.[150] It was initially created through the Companies (Amendment) Act 1990, but it was not operating in the ways that it was expected since it was criticised of being unjust[151] therefore, amendments that changed what was considered as a drawback occurred.[152] Examinership sort of promotes a pioneer thinking and it is potentially the most optimistic mechanism that this thesis has encountered. The boundaries of the Cypriot examinership, which is a model of the Irish examinership, were evaluated in Chapter 5, Section 5.5 of this thesis thus, this section explains the divergence between the Irish and Cypriot examinership. There is room for debate as to whether examinership has succeeded in Ireland, but it might be too early to generate a deduction as to whether it would be a successful mechanism in Cyprus since it has been in force for less than five years.

The Irish examinership is more akin to the USA Chapter 11 than the UK administration as administration is not management-oriented, whereas in examinership the management remain in place.[153] In this mechanism the director remains in place but an examiner who is responsible for creating the examinership plan is appointed.[154] The

[150] Irene Lynch-Fannon, Gerard Murphy, *Corporate Insolvency and Rescue* (2nd edn, Bloomsbury Professional 2012) 12.02.
[151] J Donnelly, 'Is There a Case for Corporate Rescue?' (1994) 1 Commercial Law Practitioner 8.
[152] The most significant alterations happened through the Companies (Amendment) (No. 2) Act 1999 (CA 1999) and the CA 2014.
[153] David Baxter, Tanya Sheridan, 'Irish examinership: post-eircom A look at Ireland's fastest and largest restructuring through examinership and the implications for the process' (2012) 6 Insolvency and Restructuring International 26-29.
[154] CA 2014, s 534(1).

examiner is a qualified IP in Ireland who can either be an accountant or a lawyer that passed the relevant exams. Insolvency experts are suggesting that the Irish jurisdiction does not belong to the spectrum of pro-creditor or pro-debtor as it balances the interests of both.[155] Examinership is ostensibly combining the DIP approach with procedures that displace the management of the company.[156] Lynch-Fannon and Murphy stated that by keeping the directors in place, it evokes the suspicion and dissatisfaction of creditors even though an examiner also retains some of the control and the creditors could intervene as regards the identity of the examiner. McCormack suggested that this "might create an arena for clashes of opposing egos and interests" but he also adds that this kind of behaviour has not been detected in Ireland.[157] The examiner has a certain degree of supervising role although, his/her control has a limited spectrum. Particularly, the examiner is restricted from formulating proposals about the sale of assets and/or business or the winding up of the company and s/he is restricted from undertaking executive decisions.[158] These limitations are potentially responsible for the low usage of examinership in Ireland hence, an analysis of this is vital.

In Ireland, the reckless trading provisions are available through CA 2014 s 610, which are equivalent to the wrongful trading rules in the UK. As highlighted previously[159] in this thesis the existence of these provisions is important as they are contributing to the encouragement of early restructuring. In Cyprus, it is only the fraudulent trading provisions that are active, which makes it even more difficult to persuade companies to use the Cypriot examinership. The reckless trading rules provide

[155] Michael Murphy, Grace Armstrong, 'Ireland: Corporate Recovery & Insolvency 2019' 15 May 2019 <https://iclg.com/practice-areas/corporate-recovery-and-insolvency-laws-and-regulations/ireland> accessed 04 September 2019.
[156] McCormack, *Corporate Rescue Law – An Anglo-American Perspective* (n 52) 152.
[157] Ibid 154.
[158] *Re Clare Textiles Ltd* [1993] 2 IR 213.
[159] See Chapter 2, Section 2.2, Chapter 5, Section 5.5.2 and Chapter 6, Section 6.2.1.

an infrastructure to the Irish examinership and this could further be asserting a firmly rescue-oriented model if compared to Cypriot insolvency regime.

The active involvement of the judiciary is compulsory since, amongst other things, the judge appoints the examiner and approves the plan that the examiner formed.[160] The formulation of examinership gave rise to controversial debates about its application thus, the duty of interpreting various aspects fall into the authority of the courts.[161] The courts *inter alia*, identified the operation of the process and determined the statutory purposes. A moratorium that provides a 'breathing space', of 70 days with the possibility of extension to 100 days to the company could not be absent.[162] The court has the discretional power to lift the moratorium if there have been unjust circumstances to the initiation of examinership for example. The duration of examinership makes the process less cumbersome and time-consuming in comparison to Chapter 11 that has an average endurance of two years.[163] Nonetheless, examinership is the most expensive procedure in comparison to Chapter 11 and administration, as it involves both the expenses of an expert and of the judiciary.

Examinership cases were invariably determined at the High Court, but now examinership is available for smaller companies to be ruled upon at the Circuit Court. This addition occurred because it was reported that examinership was principally preferred by large companies.[164] The purpose was to reduce the costs for smaller companies that do not have the same cash-flow as larger companies to make examinership suitable for all companies. It seems though that the expenses are still high

[160] CA 2014, s 509.
[161] Lynch-Fannon and Murphy (n 150) 12.01.
[162] CA 2014, s 534(3).
[163] Gerard McCormack, Andrew Keay, Sarah Brown, *European Insolvency Law: Reform and Harmonization* (EE Publishing 2017).
[164] Lynch-Fannon and Murphy (n 150) 13.04.

because small companies are struggling to use of examinership because they cannot afford it.[165]

There might not be enough time to complete all the aspects of the plan within less than four months that can, therefore, engender other complications. The Cypriot legislator deemed the duration of the Irish examinership short hence, the Cypriot examinership moratorium lasts for four months with the possibility of extending it to six months.[166] Even though the duration in Cyprus is longer than in Ireland, there is not be enough time to deal with all the legacy issues to bring the company back into recovery. This means that examinership in both Ireland and Cyprus, can only have an efficient outcome if there has been extensive organisation and preparation before the official entrance to the process. Without the long planning of the arrangement, the effort to have a successful examinership would be meaningless and unfruitful. Another major obstacle is the workload of the Cypriot courts,[167] which would mean that there is not be enough time to deal with the case within the time limit that is provided by the legislation.

An examinership petition is required to be accompanied by a report of an independent expert. The expert is typically the accountant/auditor who acts as the examiner of the company. The compulsory attachment of an independent expert's report on the examinership petition was one of the additions of the CA 1999 amendments. The report is of vital significance for the courts as it is used as guidance on deciding whether to grant the order of approval to the examinership plan. This report must also contain an opinion on whether examinership has a more beneficial impact on creditors and on members as a whole rather than in liquidation,[168] a statement of company affairs,

[165] Jonathan McCarthy, 'Challenges in finding the "right" approach to SME rescue: the example of reforms to the Irish examinership process' (2019) 32 Insolv. Int. 43-55, 52.
[166] CAP. 113 Part IVA, section 202H (1).
[167] Discussed in Chapter 5, Section 5.5.2.
[168] *Re Vantive Holdings* [2009] IESC 68 [3.5].

whether there is a real prospect of survival for the company and an evaluation as to the viability of a compromise or a scheme of arrangement in terms of improving the chances of rescue.[169] If the petition does not contain the independent expert's report, the courts might provide time to submit it, but the moratorium is not triggered yet. Evidence should be attached on the report that would support the opinion of the accountant that prepared it.[170] The courts have underpinned, that if the estimations of the expert regarding the prospects of survival of the company are "vague and nebulous"[171] or if there is an argumentation that lacks foundation,[172] the plan is not to be approved. Therefore, this report is causing a valuable input for the court to deduce whether the company can overcome its difficulties. The existence of this report arguably amplified the rescue perception that examinership possesses.[173]

The creation of the independent expert's was also of major importance for the Cypriot courts therefore, the legislator ensured that this provision was implemented into the Cypriot insolvency regime in 2015. The report is pivotal for the judge who is dealing with the case, since conventionally s/he does not have the financial knowledge and experience that the accountant who prepared the report has.[174] Arguably, an accountant is in a better position to estimate whether the company has a viable future.

The majority in number and in value of the claims of the creditors that are present at the meeting have to approve the plan.[175] This can be regarded as having a low threshold but the courts can cram down creditors through reversing their decision, if the judge estimates that this has been an unfair and unequitable decision for the minority.

[169] CA 2014, s 511(3).
[170] Lynch-Fannon and Murphy (n 150) 12.58.
[171] *Re Gallium Ltd* [2009] IESC 9.
[172] *Re Fergus Haynes Ltd* [2008] IEHC 327.
[173]McCarthy (n 165).
[174] See Chapter 5, Section 5.5.2.
[175] CA 2014, s 540.

There is the same requirement in Cyprus and even though examinership did not yet find success in terms of use, one would suspect that this feature could be exploited by senior creditors to the disadvantage of unsecured creditors. The courts can regulate this, but the judges in Cyprus do not have the experience to determine that yet. While most jurisdictions do not have specialist courts of insolvency, Ireland is ahead concerning insolvency matters since there is a commercial division of the High Court that has a high degree of commercial experience.[176] This signifies that the Irish courts could handle any upcoming situation that arises from the examinership petition.

The moratorium protects the company from any winding up petitions and it restricts winding up resolutions from taking effect.[177] Also, a receiver cannot be appointed while the company is in examinership, but a receiver can be ceased if s/he has been appointed three days or less prior to the submission of the examinership petition.[178] Consequently, if the receiver was appointed for example one to three days before the submission of the examinership petition, the receiver can either be stopped or s/he can only be allowed to deal with specific assets. Receivership operates in the same way that it operates in Cyprus and the UK, where the creditor needs to have a floating charge holder to be able to appoint a receiver.[179] The Cypriot Parliament regarded the period of three-days as very short thus, a space of thirty-days was enforced instead. Although this was a genuine alteration there might have been unintended reverberations.[180]

[176] McCormack, Keay and Brown (n 163).
[177] CA 2014, s 520(4).
[178] CA 2014, s 522.
[179] *Re Holidair Ltd* [1994] 1 IR 416.
[180] See Chapter 5, Section 5.5.3. for this analysis.

The availability of examinership is restricted on the basis of whether the company "is, or is likely to be unable to pay its debts".[181] It is a procedure that can function as a preventative insolvency measure since it is not only accessible to insolvent companies but also to companies that are on the verge of insolvency. The company can only utilise examinership if the court is "satisfied that there is a reasonable prospect of the survival of the company and the whole or any part of its undertaking as a going concern".[182] The formation of this object was a creation of the 1999 and 2014 amendments, as the original legislation referred to "some prospect".

Since the company rehabilitation is the focal and exclusive target of examinership, it restrains the company to this specific aim. Examinership is dedicated on rescue since its purpose emboldens the corporate rescue attempt as it is the focus of the mechanism. It deviates from the idea of having a more beneficial realisation of assets. This is because the examiner has the control over the company restructuring but s/he is forbidden from selling the business or the assets to a new company (Newco). Yet, if the company uses examinership and at the end of the day the company cannot be saved, the value of the company has probably deteriorated. That said, it is going to be impossible to at least save the enterprise even after the company exits examinership. The quantitative data analysis of this thesis indicates that the companies that went into the UK administration in the UK and achieved company rescue were 3 out of 600, while in the USA the probabilities are better as 36.7 per cent of companies were restructured.[183] Chapter 11 provides the option of selling the business of the company, which is its most common outcome.[184] It is sensible that when the option of selling the

[181] CA 2014, s 509.
[182] CA 2014, Part 10, s 509(2).
[183] See Chapter 2, Section 2.4.1 for the administration analysis and for the comparison with the USA see Chapter 6, Section 6.2.2.2.
[184] McGlaun (n 101).

business to a Newco or realising the assets is absent, problems would be created. The fact that the examiner lacks the option of saving the business was apparently an impediment for the progress of a number of examinership cases.[185] Costello J held in *Clare Textiles*:

> "[t]he examiner has no authority to prepare proposals involving the sale of the company's assets and its business or its liquidation and in my opinion the court has no power to confirm proposals under s 24 which do not provide for the survival of the company and at least part of its undertaking as a going concern. … The section must be construed in the light of the earlier sections of the Act … the examiner was required to exercise the powers he obtained so that he could fulfill his statutory functions."

Irrespective the various obstacles of this process, the aftermath of examinership cases seems encouraging. According to the Business in Ireland 2017 Annual Report, between 2007-2016, 420 companies used examinership,[186] where the 56 per cent of those companies are trading as going concerns, 23 per cent were dissolved and the 20 per cent of those companies were under liquidation.[187] However, the outcome results should be compared with the extent of usage of examinership. In 2017, only 29 examinerships were recorded, which was the 3 per cent of all corporate insolvencies in Ireland for the

[185] *Clare Textiles*, 220–221; *Re Wogan's (Drogheda) Ltd (No 2)* (1992) ICLR 692; *Re Antigen Holdings Ltd* [2001] 4 IR 600, 603; Lynch-Fannon and Murphy (n 150) 13.24.
[186] The type of companies that ordinarily use examinership in Ireland are wholesale or retail, professional services and companies from the tourism industry.
[187] Business in Ireland 2017 Annual Report <http://www.vision-net.ie/news/2017-annual-review-report> accessed 06 September 2019.

year.[188] The number of examinerships has increased in 2018 since 39 companies used examinership. 17 of those companies belong to the same group, which means that the figures drop to 23 companies (22+1(17) = 23), that is the 3 per cent of all corporate insolvencies for 2018. [189] The 2019 figures have not been encouraging since in the first quarter of 2019 only 8 examiners were appointed, that is the 4 per cent of all insolvencies for that quarter.[190] Hence, the underuse of examinership is an issue of concern for Ireland. In comparison to the USA the 30 per cent of all corporate insolvencies choose the path of restructuring, while in the UK 1 out of 7 companies choose restructuring.[191] The statistics about the examinership outcome suggest that this mechanism has been successful in Ireland in the turnaround of companies but, the insufficient use examinership does not really reflect a success in the real sense of the word.

However, while in Ireland there have been attempts to utilise examinership where it could have an efficient outcome, there have not been any such endeavours in Cyprus thus the Cypriot examinership is currently idle. As examinership is a court-driven procedure it requires the constant involvement of the courts, but when considering the current problems with the Cypriot courts that examinership is not tailored for Cyprus. What could further countenance this is the fact that there is space for misuse, which practically harmed the accountability of the Cypriot examinership before it was even brought into practice.

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[188]Corporate insolvencies in Q1 2018 total 188, down 14% when compared with Q1 2017 <https://www2.deloitte.com/ie/en/pages/about-deloitte/articles/insolvency-stats-Q1-2018.html> accessed 06 September 2019.

[189] Deloitte Insolvency Statistics - A year in review 2018 <https://www2.deloitte.com/ie/en/pages/about-deloitte/articles/insolvency-stats-year-in-review-2018.html> accessed 06 September 2019.

[190]8 out of 10 companies entering insolvency in Q1 2019 established more than five years ago <https://www2.deloitte.com/ie/en/pages/about-deloitte/articles/q1-2019-insolvency-statistics.html> accessed 06 September 2019.

[191] Deloitte Insolvency Statistics - A year in review 2018 (n 188).

6.4 Conclusion

The evaluation of other jurisdictions regarding rescue other than the UK and Cyprus broadened the conception of reform ideas. Also, it has been comprehended that the successfulness of rescue could depend on the perception of the public and the motivation of directors. Chapter 11 is drawing the attention of lawmakers and commentators due to the DIP financing attribute, which is arguably significant for the benefit of the company and eventually of creditors. It cannot be stressed enough how important financing agreements are for Chapter 11, since if they did not exist it could not have gained the same scope and reputation. Company rescue is the cornerstone of Chapter 11, but the creditor control is undermining this. It is arguable whether the transplantation of Chapter 11 would have had the same results in Cyprus or in the UK. The changes that were implemented on administration and on Chapter 11 since their introduction brought them closer together as it seems that they are meeting in the middle.[192]

Examinership has a high rate of company survivals, but it is not the usual option for Irish companies. The extent of utilisation in Ireland is inconsistent with the attempt to ameliorate the procedure in 2014. Examinership is the procedure that is most prone to rescue, however, those particular features that are encouraging rescue are the obstacles to the progress of it. Currently, the Cypriot examinership is not chosen by companies but if it begins to grasp attention, it will possibly encounter the same issues that the Irish examinership is experiencing in practice, issues that were discussed above.

Importantly, the directive that was adopted in June 2019 by the European Council includes several characteristics of Chapter 11. An attempt of harmonising the

[192] Sarah Paterson, 'Rethinking the Role of the Law of Corporate Distress in the Twenty-First Century' (2016) 366 Oxford Journal of Legal Studies 697–723.

rescue attitude between member states of the EU is important, although they have the flexibility of adjusting the directive's articles in accordance with their legal background. It indeed has a lot of features analogous to Chapter 11 such as rescue financing, incorporating DIP in a way that would encourage early filing and stay. According to McCormack "The Restructuring Directive Proposal in a sense is Europe's answer to Ch.11, but it is a work in progress rather than a fully finished product."[193] This is an attempt to replicate various characteristics of Chapter 11, but since each member state has the freedom of transposing those rules to a minimum, it could have a varying effect from Chapter 11. A few rules that the directive has are already present in some of the legislations of the EU member states. Hence, it remains to be seen how the member states will apply the directive into their national legislation and what the outcome will be.

[193] McCormack, 'Corporate restructuring law - a second chance for Europe?' (n 3).

Chapter 7 – Epilogue

7.1 Synopsis and arguments

The broad research question of this thesis is to address the effect of corporate rescue procedures in the United Kingdom (UK) and determine which functions can act as a paradigm for the development of the Cypriot corporate insolvency rescue regime. All chapters of this thesis are interlinked for this deduction, since various sub-questions needed to be addressed for a cognitive answer of the main question. These rescue procedures must evolve to be compatible with the business, economic and cultural needs of the time. Possible changes that are capable of ameliorating administration and company voluntary arrangements (CVAs) in the UK were identified as well as the changes that could make the Cypriot procedures more effective. Various sub-issues emerged through researching these corporate rescue mechanisms that include *inter alia*, rescue finance, the response of creditor/debtor-oriented mechanisms and the impact of debtor-in-possession mechanisms to creditors and directors. The corollary of investigating these attributes was to include the United States of America (USA) Chapter 11 in the analysis. This aimed at determining aspects that could be mirrored from Chapter 11 to the insolvency regime of the UK and/or Cyprus. A comparison between the Cypriot examinership and Irish examinership was important, because although they are almost identical, the attitudes behind these tools diverge. The aforementioned were vital for evidencing whether there should be calls for reforming the procedures in Cyprus. The novelty of this research lies within the comparator jurisdictions and their empirical evaluation.

The rehabilitation of the entity is seemingly an ideal outcome for a rescue mechanism. Chapter 2 challenges this view as the analysis led to the conclusion that a

business rescue could have more beneficial results to stakeholders collectively than in a company rescue. Business rescue is a more common outcome of administration than company rescue which has been reinforced by the empirical analysis of the author of this thesis and past empirical researches.[1] Some theories such as the Darwin theory augment the value of the business rescue. The standpoint of banks, directors, employees and unsecured creditors provides that a business sale could balance their interests. Most interviewees of this research underpinned this argument but a hesitation that is attached to cultural attitudes was manifested. The contemplation of business rescue having a more efficient collective outcome – especially in jurisdictions that are creditor-oriented – is interlinked with the discussions that follow in the next chapters.[2]

CVAs proved to be useful for high street retailers, restaurateurs and football clubs hence, this tool is possibly more suitable for larger companies. Chapter 3 questions whether the intention of these companies is in reality to compromise rents.[3] Through some recent decisions, the judiciary attempted to address this issue but there is still space for challenges.[4] CVA with a moratorium should be revised, as even though it aimed at smaller companies it is not accessible to them. Large companies need the moratorium while smaller companies cannot use it due to the extensive costs.

Business sale and/or the realisation of assets is the main focus of administration rather than the rehabilitation of the entity. Is this really promoting the more advantageous outcome for most stakeholders? In administration, more than half of

[1] See Chapter 2, section 2.4.1; Sandra Frisby, 'Interim Report to the Insolvency Service on Returns to Creditors from Pre- and Post-Enterprise Act Insolvency Procedures' (July 2007); Alan Katz, Michael Mumford, 'Study of administration cases' (2007) 20 Insolv. Int. 97-103.
[2] See Chapter 2, Section 2.4.2.
[3] See Chapter 3, Section 3.7.
[4] *Debenhams CVA in Discovery (Northampton) Ltd and others v. Debenhams Retail Ltd and others* [2019] EWHC 2441 (Ch); *Re SHB Realisations Ltd (formerly BHS Ltd) (in Liquidation), Wright v. Prudential Assurance Co Ltd* [2018] EWHC 402 (Ch).

preferential creditors and 38 per cent of secured creditors received full returns.[5] Although when the Enterprise Act 2002 (EA 2002) was initially implemented these creditors felt disenfranchised, now they seem satisfied with the procedure. This is mainly due to their realisation about the equivalence of administrative receivership with administration. It is evidently a process that unsecured creditors cannot benefit from. It is questionable though whether unsecured creditors could have been in a better position in any other process.[6] Chapter 4 has highlighted some aspects that are potentially compromising the upshot of administration such as the misuse of the moratorium and the criticism of pre-packaged administrations (pre-packs). This thesis is of the view that it is better to enhance the current administration moratorium and extend the CVA with a moratorium to large companies rather than providing another tool that is susceptible to failure. Mindful of the sunset clause of May 2020 that bounds the Government to reconsider whether action needs to be taken regarding phoenix trading during administration,[7] this thesis suggests that the legislator should review the possibility of legislating pre-packs and transforming the pre-pack pool and the viability review into mandatory forums.[8]

Chapter 5 determines the effectiveness of examinership, schemes of arrangement and receivership that are all included in the Cypriot Companies Law, Chapter 113 (CAP. 113). The evaluation of CVAs and administrations in the UK broadened the horizons of this research, regarding the understanding of corporate rescue. This gave way to discussions that are intertwined with the previous chapters since for instance the issue of company/business rescue resurfaced. The conclusion

[5] See Chapter 4, Section 4.2.2.
[6] Andrew Keay, 'The future for liquidation in light of the Enterprise Act reforms?' [2005] J.B.L. 143-158, 150.
[7] Insolvency Act 1986 (IA 1986), Sch B1, para 60A.
[8] Chris Umfreville, 'Review of the pre-pack industry measures: reconsidering the connected party sale before the sun sets' (2018) 31 Insolv. Int. 58-63.

about examinership is that – even though it is arguably early to gauge its effectiveness – a debtor-oriented process cannot survive in a jurisdiction that has always favoured creditors. This chapter identified that receivership is prevalent mainly because banks trust it as they are in more control.[9] Examinership should be subject to changes if a proper functionality is the future target.[10] That said, it is assumed – although some caveats are considered – that administration could have been more compatible to the Cypriot jurisdiction.[11] The 2015 amendment on the schemes of arrangement about the reduction of the creditor's votes to a simple majority was a bold move that could ease the process. The 2015 changes on the schemes of arrangement and on the introduction of examinership are susceptible to misuse, thus they should potentially be revisited in the future.[12] This analysis also led to discussions that are linked to the Cypriot legal infrastructure. Consequently, although some recommendations were highlighted, their accomplishment is somewhat challenging. The legislator will have to review the insolvency framework regime again to be in line with the DIRECTIVE (EU) 2019/1023 (the 2019 directive). This could be an opportunity of taking into consideration the implementation of rules that are beyond the minimum requirement of the 2019 directive.

Chapter 6 indicates that each jurisdiction is structurally built to be compatible to certain attributes of the legislation. The management's 'reward' of remaining in place and their hands-on knowledge about the company facilitate an easier access to rescue.[13] Other aspects of Chapter 11 that enhance rescue outcomes is the cram down mechanism that forces difficult creditors to cooperate and financing agreements that gives easy

[9] See Chapter 5, Section 5.3.2.
[10] Chris Iacovides, 'One Way Road to the Death of Ailing Companies – the New Receivership Bill' CRI Group, 2016 < http://www.crigroup.com.cy/wp-content/uploads/2018/06/Receivership-Bill.pdf> accessed 13 October 2019.
[11] See Chapter 5, Section 5.6.
[12] See Chapter 5, Section 5.4.1 and 5.5.3.
[13] See Chapter 6, Section 6.2.1.

access to funds.[14] The evolution of these attributes altered to a certain extent the distribution of authority between debtors and creditors.[15] An entity rehabilitation is not an unfamiliar occurrence in the USA, but not as accustomed as one would expect. It seems that Chapter 11 and administration meet somewhere in the middle. If a direct replication of the financing agreements is triggered in the UK, their compatibility is doubtful. The attempt to differentiate the Irish examinership that is available to smaller and large companies was not as fruitful as it was expected. The obstruction of business rescue through the Irish examinership provides limitations to the outlook of its outcome.[16] This is a difficulty that is also expected to be triggered in Cyprus.

7.2 Deductions about the Cypriot corporate rescue regime

Several proposals have been set out through this thesis for the Cypriot insolvency regime to grow. The Cypriot legislator will have the opportunity to re-evaluate examinership to explore the compliance of the restructuring regime with the 2019 Directive. The UK insolvency regime operates as a pragmatic paradigm for addressing the problems of the Cypriot insolvency regime. The deductions of this thesis about ameliorating the Cypriot rescue regime have been enhanced from the elucidation of the UK's success and failure stories. The extensive involvement of creditors in the UK corporate insolvency regime and the censures about the curtailed rescue regime before the EA 2002 led to developments that produced efficiency and simultaneously space for improvement. These amendments were an important source of analysis for the thesis that led to discussions about addressing the problems that might arise and determining

[14] See Chapter 6, Section 6.2.3.
[15] See Chapter 6, Section 6.2.2. and 6.2.3.
[16] See Chapter 6, Section 6.3.1.

which aspects could work better in Cyprus. For instance, an out-of-court option – that was also allowed in administration through the EA 2002 – is pivotal for the course of action of the Cypriot examinership. The deterrent of this action is the problem on administration e-filings that is of current concern for the English courts. Rescue finance is substantial for rescue procedures to evolve as its availability would not obstruct companies from exploiting examinership in the prospective future. The evaluation of the effect of DIP financing agreements and cram down in Chapter 11 was valuable for keeping Cyprus in line with the 2019 Directive, but also for persuading the UK to remain competitive to foreign companies. The difficulty of achieving company rescue is underpinned through juxtaposing it with business rescue, which effectively aids in addressing the research question of this research. The sale of the business to a new company is not allowed through the Cypriot examinership. The exegesis of this issue through examining the Irish examinership was key as the underperformance did not enable this problem to surface in Cyprus yet.

As there have been various incidents of intentional and unintentional exploitation in the UK, the analysis of the two jurisdictions was paralleled. Therefore, this thesis highlighted methods that could minimise the misuse of mechanisms that engender the deterioration of the perception that foreign companies have about the regime. If the right changes are undertaken, Cyprus can even become the new restructuring hub in the European Union, since the UK's position will be compromised after the UK procedures cease to be recognised.

7.3 Can a company rescue procedure work equally well for both small and medium-sized enterprises (SMEs) and large corporations?

Small and medium-sized enterprises (SMEs) in both the UK and Cyprus reach on average the 99.99 per cent of all businesses.[17] The same procedures usually apply for all types of companies in both the UK and Cyprus with the exception of CVAs with a moratorium.[18] The formation of this process targeted smaller companies, but the sporadic use of the process is happening because it is burdensome and thence costly.[19] Most of the recommendations of this thesis were about making the procedures more accessible to SMEs. At the same time, a procedure that is beneficial to larger companies is necessary for the preservation of the trustworthiness and credibility of any insolvency framework.

The recent failure of large companies that include Carillion plc (Carillion), British Steel Ltd (British Steel)[20] and Thomas Cook UK Plc (Thomas Cook) created doubts as to the spectrum of capabilities of administration in terms of large company rescue. In other words, this practice generates uncertainties as to whether administration can have the same effect on different company sizes. These companies went into compulsory liquidation, where an Official Receiver (OR) was appointed.[21] The initial conjecture was that since these companies were in an irreversible insolvency state,

[17] UK Small Business Statistics <http://www.fsb.org.uk/media-centre/small-business-statistics> accessed 04 November 2019; European Commission, '2018 SBA Fact Sheet' <https://ec.europa.eu/docsroom/documents/32581/attachments/6/translations/en/renditions/native> accessed 04 November 2019.
[18] IA 1986, Sch A1.
[19] Harry Rajak, *Company Rescue and Liquidation* (3rd edn, Sweet & Maxwell 2013) 59.
[20] *Re British Steel Ltd* [2019] EWHC 1304 (Ch).
[21] Andrew Keay interviewed by Samantha Gilbert, 'Thomas Cook collapse—is court-ordered liquidation the new administration?' 30 September 2019 <https://www.lexology.com/library/detail.aspx?g=26e1801a-f5d4-4686-8c46-ce4fbff21ec3> accessed 18 December 2019.

administration could not be an option.[22] The answer is more complex rather that simplistic.

Big accounting firms declined the request of the company lenders to undertake such a risky appointment. As in all three large companies there have been several environmental, health and safety issues, no prospect administrator was willing to take on that role without disclaimers. In compulsory liquidation as opposed to administration, liquidators can disclaim the assets that contain obligations related to environment, health and safety.[23] This was also to the advantage of creditors as obligations would be transferred from them to the government. In Carillion, these firms were wary of taking responsibility also because there were no meaningful assets that they could rely on for repayment.[24] The same private accounting firms accepted the request by the OR to act as special managers though since they would not be in the same level of jeopardy.

Furthermore, asset-based lenders refused to fund an administration as they believed that their chances of receiving any returns would be drained. As an OR took over, the payment of fees is guaranteed by the taxpayer. Arguably, floating charge holders had a rogue plan, in which the liability for any costs would be detached.[25] This would incentivise further practice equivalent to this, whereby asset-based lenders could exploit the situations through avoiding the appointment of administration and impliedly pursuing a compulsory liquidation. This is linked to the fact that the administration costs are top-sliced from the floating charge assets.[26] The government would not have agreed

[22] David Milman, 'UK Restructuring Law: Recent Developments Considered' (2019) 418 Co. L.N. 1-5.
[23] *Re Celtic Extraction Ltd* [1999] 2 BCLC 555.
[24] Matthew Vincent, 'Why Carillion has gone into liquidation rather than administration' Financial Times, 14 January 2018, <https://www.ft.com/content/a4dd80be-f9f1-11e7-a492-2c9be7f3120a> accessed 09 December 2019.
[25] Andrew Keay, Peter Walton, 'British Steel: is it a wind up?' (2019) 12 C.R. & I. 125-128.
[26] IA 1986, s 176ZA; For issues related to justice and fairness of this practice see Chapter 2, Section 2.5.

to fund the continuation of trading while the company was in liquidation if this was not a matter of public interest.

All three companies and particularly Carillion are massively public interest driven thus, the lights cannot go out effortlessly. These companies were of the perception that they were too big to fail and that due to the nature of their businesses, banks, bondholders, and other stakeholders would always support them. The fact that with Carillion a lot of sectors – such as hospitals, police stations, schools, fire stations and military – depended on its continuance of trading, it would have been a national security risk.[27] Arguably, the situation in Carillion was different due to the type of business. The judiciary accentuated that when then there is a matter of public interest, the continuance of trading in liquidation is justifiable.[28]

Are these cases too peculiar that they should be treated in isolation, or is this becoming a trend that should grasp the attention of the legislator? This is a sceptical question as the reasons that led these companies in liquidation are synthesised. Calls for attention should be undertaken as Milman emphasised: "it is hardly a vote of confidence in the administration process".[29] A business trade and/or sale is not a purpose that should be pursued in liquidation,[30] which shows that this is an unsettled issue that needs to be revisited. It is concluded that procedures that are available to SMEs might not be suitable for larger companies and vice versa. Steps that could be taken is to differentiate somehow the attributes of procedures in which large companies and SMEs would be eligible to. Although there is nothing unusual in focusing on small companies since the

[27] Federico Mor, Lorraine Conway, Djuna Thurley, Lorna Booth, 'The collapse of Carillion' (14 March 2018) House of Commons Briefing Paper, Number 8206.
[28] *Faryab v. Smith* [2001] BPIR 246; *Whitehouse v. Wilson* [2006] EWCA Civ 1688.
[29] Milman, 'UK Restructuring Law: Recent Developments Considered' (n 22).
[30] The liquidator has the authority to do this only in circumstances where a more effective liquidation would occur; IA 1986, Sch 4, para 5.

aim of the Companies Act 2006 was to "think small first",[31] a differentiation between rescue procedures that are formally available to SMEs and large companies is a potential proposition for the legislator to put forward. For this to be successful other provisions that would facilitate their operation should be examined in future research. A key aspect that will certainly seize the attention of the government is rescue finance. As such various components that give incentives for further research regarding debt finance of SMEs are highlighted further.

[31] Danielle Harris, 'Has the new Companies Act helped small business?' The Times, 29 October 2009.

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APPENDIX A

Semi-structured Interview Questions

UK

1. Should the administration procedure in Schedule B1 of the Insolvency Act 1986 be streamlined? If yes, what changes do you suggest?
2. Do you believe that the pre-pack pool and the viability review should become compulsory? Do you think that pre-packs should be the subject of specific legislation?
3. Do you believe that the substitution of administrative receivership by administration produced generally a better outcome for stakeholders?
4. CVAs are unattractive to SMEs. Do you believe that they should be rejuvenated? If yes, what kind of reforms would you recommend?
5. Do you believe that the so-called "rescue" procedures in the UK should become more rescue oriented rather than having debt return to creditors as their core aim? What might be the reaction of creditors (banks) to any such change?
6. What is the average cost of a corporate rescue procedures? Is it more advantageous for the creditors to go through a rescue procedure than directly liquidate the company?
7. How do companies finance the insolvency rescue procedures that are provided for by the legislation? To what extent do companies go into factoring/invoice agreements to fund these procedures?
8. What is your opinion about the plans to move forward with a pre-insolvency moratorium?
9. What is your opinion on the recent proposals on the prescribed part and preferential status of the Crown?

Cyprus

1. In your opinion, do the 2015 reforms that were made to the corporate insolvency law in Cyprus work effectively?
2. What are the challenges of the procedures of examinership, compulsory liquidation and schemes of arrangement?
3. What further reforms to corporate insolvency law in Cyprus would you like to see made?
4. What is your opinion on receivership and what is the effect of this procedure on companies?
5. Is examinership more suitable for large companies or small companies? Is 4 months with the possibility of 2 months extension enough time for the examiner to restructure the company? More extension for larger companies?
6. Are you aware whether there will be a training for judges in Cyprus on how to deal with insolvency cases?
7. Do you believe that UK administration would have been a better procedure for Cyprus that examinership?
8. Do you believe that if wrongful trading provisions were included in the Cypriot legislation, these rescue procedures would function more effectively?
9. How do companies finance the corporate insolvency procedures that are provided by the legislation? To what extent do companies go into factoring/invoice agreements to fund these procedures?
10. What is the average cost of corporate rescue procedures? Is it more advantageous for the creditors to go through a rescue procedure than directly liquidate the company?

APPENDIX B

Participant information sheet

My name is Sofia Ellina (Tel.: +44 7599411745, Email address: s.ellina@lancaster.ac.uk) and I am a PhD student at Lancaster University and I would like to invite you to take part in a research study about – 'A rescue culture in Insolvency Law: A comparative socio-legal analysis of the approach of UK and Cyprus.'

Please take time to read the following information carefully before you decide whether or not you wish to take part.

What is the study about?

Administration and company voluntary arrangements, per the Insolvency Act 1986, can be used by economically distressed companies in the United Kingdom(UK) as rescue tools. Schemes of arrangement is another legal mechanism provided by Companies Act 2006 that facilitates the restructuring of companies. In Cyprus ailing companies have three legal options that operate as alternatives to liquidation: receivership, schemes of arrangement, and examinership.

In May 2015, the Parliament of Cyprus introduced some amendments to insolvency law which had the purpose to modernise the system and promote a rescue culture. Companies Law was amended with the application of the examinership procedure. Receivership and schemes of arrangement pre-existed but examinership was implemented in the legislation after the amendment of Companies Law (CAP. 113) in 2015. Administration and

examinership both have a primary common objective, which is to save the company, but their differences are significant and will be illustrated.

A key aim of this project is to evaluate Cyprus's current position and options in relation to corporate rescue with the influence of the efficacy of corporate rescue mechanisms in the UK and other jurisdictions. This necessitates a comparison with various jurisdictions such as United States of America and Ireland in order to be in the position to recommend legal transplants for the rescue culture in the UK and Cyprus. Also, the efficiency of the corporate models is evaluated through an empirical research that includes quantitative data collection and conduct of interviews in both the UK and Cyprus.

Why have I been invited?

I am interested in understanding how efficient are the corporate rescue procedures in Cyprus and the UK and I strongly believe that my research will be enriched by interviewing you.

I would be very grateful if you would agree to take part in this study.

What will I be asked to do if I take part?

If you decided to take part, this would only involve an interview with questions related to Insolvency Law and particularly corporate rescue.

What are the possible benefits from taking part?

Participants may also benefit from quantitative data that will be provided to them for comments in the course of the interview.

Do I have to take part?

No. It's completely up to you to decide whether or not you take part. Your participation is voluntary. If you decide not to take part in this study, this will not affect your position in the company or the service.

What if I change my mind?

If you change your mind, you are free to withdraw at any time during your participation in this study. If you want to withdraw, please let me know, and I will extract any data you contributed to the study and destroy it. Data means the information, views, ideas, etc. that you and other participants will have shared with me. However, it is difficult and often impossible to take out data from one specific participant when this has already been anonymised or pooled together with other people's data. Therefore, you can only withdraw up to 2 weeks after taking part in the study

What are the possible disadvantages and risks of taking part?

It is unlikely that there will be any major disadvantages to taking part. I would like to inform you that by taking part will mean investing minimum 60 minutes for an interview.

Will my data be identifiable?

After the interview, only I, the researcher conducting this study will have access to the data you share with me.

I will keep all personal information about you (e.g. your name and other information about you that can identify you) confidential, that is I will not share it with others. I will anonymise any audio recordings and hard copies of any data. This means that I will remove any personal information.

How will my data be stored?

I will be the sole person who will have access to the data. I will retain the data for a minimum of ten years and I will not use the data for anything else than my research.

Data will be stored on encrypted and password protected external drives as well as university drive.

How will we use the information you have shared with us and what will happen to the results of the research study?

I will use the data for academic purposes only. This will include my PhD thesis and other publications, for example journal articles. I may also present the results of my study at academic conferences.

When writing up the findings from this study, I would like to reproduce some of the views and ideas you shared with me. When doing so, I will only use anonymised quotes (e.g. from our interview with you), so that although I will use your exact words, you cannot be identified in our publications.

If anything you tell me in the interview (or other data collection method) suggests that you or somebody else might be at risk of harm, I will respond according to the English Law.

Who has reviewed the project?

This study has been reviewed and approved by the Faculty of Arts and Social Sciences and Lancaster Management School's Research Ethics Committee.

What if I have a question or concern?

If you have any queries or if you are unhappy with anything that happens concerning your participation in the study, please contact my supervisors Dr Kayode Akintola (Tel: +44 (0)1524 593055, k.akintola@lancaster.ac.uk**) or Professor David Milman (Tel: +44 (0)1524 594614,** d.milman@lancaster.ac.uk**).**

If you have any concerns or complaints that you wish to discuss with a person who is not directly involved in the research, you can also contact the Head of the Law School Professor Alisdair Gillespie (Tel: +44 (0)1524 593706, Postal address: Lancaster University Law School, Bowland North, Lancaster University, Lancaster, LA1 4YN, United Kingdom, Email address: a.gillespie@lancaster.ac.uk,)

Thank you for considering your participation in this project

APPENDIX C

CONSENT FORM

Project Title: A rescue culture in Insolvency Law: A comparative socio-legal analysis of the approach of UK and Cyprus.

Name of Researcher: Sofia Ellina
Email: s.ellina@lancaster.ac.uk

Please tick each box

1. I confirm that I have read and understand the information sheet for the above study. I have had the opportunity to consider the information, ask questions and have had these answered satisfactorily ☐
2. I understand that my participation is voluntary and that I am free to withdraw at any time during my participation in this study and within two weeks after I took part in the study, without giving any reason. If I withdraw within two weeks of taking part in the study my data will be removed. ☐
3. I understand that any information given by me may be used in future reports, academic articles, publications or presentations by the researcher, but my personal information will not be included and I will not be identifiable. ☐
4. I understand that my name/my organisation's name will not appear in any reports, articles or presentation without my consent. ☐
5. I understand that any interviews will be audio-recorded and transcribed and that data will be protected on encrypted devices and kept secure. ☐
6. I understand that data will be kept according to University guidelines for a minimum of 10 years after the end of the study. ☐
7. I agree to take part in the above study. ☐

_____	_____	_____
Name of Participant	Date	Signature

I confirm that the participant was given an opportunity to ask questions about the study, and all the questions asked by the participant have been answered correctly and to the best of my ability. I confirm that the individual has not been coerced into giving consent, and the consent has been given freely and voluntarily.

Signature of Researcher /person taking the consent_____ Date _____ Day/month/year

One copy of this form will be given to the participant and the original kept in the files of the researcher at Lancaster

University

APPENDIX D

Interviewee no.	Date	Location	Profession	Firm type
1	04.12.2018	By phone in the UK	Credit Manager	
2	14.12.2018	Leeds, UK	IP	Big four
3	21.12.2018	Nicosia, Cyprus	IP	Insolvency Firm
4	03.01.2019	Nicosia, Cyprus	Lawyer x 3	Law Firm
5	10.01.2019	Nicosia, Cyprus	Lawyer	Law Firm
6	11.01.2019	Nicosia, Cyprus	IP	Big Four
7	15.01.2019	London, UK	Lawyer/Academic	Law Firm
8	19.01.2019	London, UK	IP	Big Four
9	28.01.2019	Nicosia, Cyprus	Lawyer	Law Firm