



**Lancaster University**  
MANAGEMENT SCHOOL

**Lancaster University Management School**  
**Working Paper**  
**2003/097**

**Comparative Study Of Administration And Administrative  
Receivership As Business Rescue Vehicles (Executive  
Summary)**

A Katz and M J Mumford

The Department of Accounting and Finance  
Lancaster University Management School  
Lancaster LA1 4YX  
UK

©A Katz and M J Mumford  
All rights reserved. Short sections of text, not to exceed  
two paragraphs, may be quoted without explicit permission,  
provided that full acknowledgement is given.

The LUMS Working Papers series can be accessed at <http://www.lums.co.uk/publications>  
LUMS home page: <http://www.lums.lancs.ac.uk/>

**Comparative Study Of Administration And Administrative Receivership As  
Business Rescue Vehicles (Executive Summary)**

**August 2003**

**Alan Katz and Michael Mumford  
Research Fellows - ICRA - Lancaster University**

©

**With kind permission of the Centre for Business Performance the executive  
summary of our study is available on this website. To obtain a copy of the full  
report on our study, please contact the Centre at Chartered Accountants' Hall,  
Moorgate Place, London EC2P 3BJ ( [www.icaew.co.uk/cbp/](http://www.icaew.co.uk/cbp/) ) Tel 020 7920 8634.**

**Comparative study of administration and administrative receivership as  
business rescue vehicles. August 2003. Alan Katz and Michael Mumford**

**Research Fellows - ICRA - Lancaster University**

<u>Section</u>	<u>Index and summary (of full paper)</u>
1	Funding and refereeing of project
2	Executive summary
3	Abbreviations
4	Background to project and legislative changes since commencement
5	Principal differences between AR and admin
5.1	Differences of principle
5.2	Differences of procedure
6	Summary of the debate
7	Factors determining choice of procedure and identification of “badged” cases
8	Research methodology
8.1	Sample sizes and coverage
8.2	Preliminary questionnaires and analysis
8.3	Preliminary questionnaires - admin cases
8.4	Preliminary questionnaires - AR cases
8.5	Supplemental questionnaires and interviews
8.6	Supplemental questionnaires - admin cases
8.7	Supplemental questionnaires - AR cases
9	Principal findings
9.1	Admin has been catching up on AR
9.2	Incidence of each procedure by size of firm
9.3	Case badging
9.3.1	AR case control considerations
9.3.2	AR case badging - delay / speed of appointment considerations
9.3.3	Comparative cost
9.3.4	Veto of administration by appointment of AR
9.3.5	Additional powers of administrator compared with AR
9.3.6	AR cases - new tax considerations arising from Finance Act 2003
9.4	Admin case badging - preliminary considerations
9.4.1	Absolute admin badging - no floating charge - Cork Report objective
9.4.2	Admin cases where there was a choice of procedure
9.4.3	Admin CVA badging
9.4.4	Admin CVAs - company and business rescue
9.4.5	Admin business reasons badged cases
9.4.6	Unbadged admin cases
9.4.7	Admin cases where charge holders amenable to an reasonable procedure
9.4.8	Unbadged admin cases - comparative cost

Section    Index and summary (ctd)

- 10            Conclusions and policy implications
- 10.1        Admin trends - relevance of abolition of AR
- 10.2        Further streamlining of admin since July 2001 White Paper proposals
- 10.3        Changes in position of floating charge holders
- 10.4        Additional costs of admin over AR
- 10.5        Administration as company or business rescue vehicle
- 10.6        Anomalous new tax consideration
- 10.7        Conduct inference of EA02 appointment procedure compared with IA86 veto
- 10.8        Extension of powers of admin/r – new conflict and ethical issues
- 10.9        Cost and availability of finance

Notes        Footnotes

- Appx 1     Admin preliminary questionnaire
- Appx 2     AR preliminary questionnaire
- Appx 3     Admin CVA cases - questionnaire
- Appx 4     Admin unbadged cases - comparative cost questionnaire
- Appx 5     AR urgent appointment cases - questionnaire
- Appx 6     AR unbadged cases - comparative cost questionnaire
- Appx 7     Summary of EA02 changes relevant to this paper

**Comparative study of administration and administrative receivership as  
business rescue vehicles. August 2003. Alan Katz and Michael Mumford  
Research Fellows - ICRA - Lancaster University**

**1 Funding and refereeing of project**

We wish to acknowledge the funding provided by the P D Leake trust (a charity associated with the Centre for Business Performance of the Institute of Chartered Accountants in England and Wales). In addition to the referees nominated by the Centre, we would also like to thank professional referees nominated by the Association of Business Recovery Professionals (ABRP - R3) who have provided valuable advice during the planning and development of the project. We also gratefully acknowledge observations on our findings by practitioner members of ABRP – R3 and by bankers and others involved in consultations on law reform.

**2 Executive summary**

**2.1 Purpose of study and changes to focus**

There continues to be debate on whether, in insolvency cases where there is an effective choice between administration and administrative receivership, either procedure is preferable (which we have defined in terms of welfare - net realisations) to the other. The study is intended to provide empirical evidence to assist the debate.

We had intended our work to be based on the Insolvency Act 1986 (IA 1986) regime, having planned our project and started work prior to the 2001-2 law reform consultation. This consultation preceded the implementation, expected in September 2003, of the relevant parts of the Enterprise Act (EA 2002). Section 250 of EA 2002 will prohibit the appointment of an administrative receiver, but only in respect of new floating charges created after the implementation date. We have continued our comparative work on the premise that there will for many years be a substantial number of cases where there could be an effective choice of procedure. We have also extended the scope of our work to consider the likely effects of, and inform the debate on, the changes that are being introduced by EA 2002.

Having regard to the planned legislative changes, we published in February 2002 our preliminary findings based on an analysis of initial questionnaires to insolvency practitioners in respect of administration and administrative receivership case appointments made during the calendar year 2000. Our preliminary paper may be found on the ICAEW and ABRP- R3 websites. The principal findings from our preliminary paper are included and developed in this paper.

In light of the legislative changes, we refocused our supplemental work to concentrate primarily on those cases that went the administrative receivership route. The purpose is to ascertain whether, and if so to what extent, one might expect realisations to be lost and costs to be increased by the abolition of administrative receivership. We also examined evidence on whether, where administration was considered the appropriate procedure, the forecast benefits unique to administration are in likely in practice to be achieved.

## **2.2 Samples and methodology**

Our findings are based on responses to questionnaires sent to insolvency office holders on initial random samples of 50% of all administration cases and 20% of all administrative receivership case appointments in the calendar year 2000 [1]. These were samples of around 180 cases for each procedure (treating groups as one case). Details of the response rates, methodology and supplemental questionnaires and analysis are given at section 8 of this paper.

## **2.3 Principal findings - general**

### **2.3.1 Administration has been catching up on administrative receivership**

Administration has been less widely used than administrative receivership since administration was introduced by IA 1986. However, the ratio of administrations to administrative receiverships has steadily increased from under 10% to over 25% of total cases during the 1990s. It has continued to increase prior to and since the debate on EA 2002, to 40 % in early 2003 and just topping 50% in the month of June 2003. This trend is further analysed at section 9.1. It appears to indicate that practitioners

and floating charge holders have become increasingly willing to consider administration to be an acceptable alternative to administrative receivership, a suggestion that was confirmed during our interviews with practitioners and bankers.

### **2.3.2 Incidence of each procedure by size of firm**

Although not directly relevant to our research, our initial samples have enabled us to analyse appointments by size of firm. There was in 2000 a statistically significant difference in concentration of administrative receiverships within the six largest insolvency practices and of administrations within the smaller practices. The statistical analysis is given at section 9.2. These concentrations reflecting specialisation in bank sourced work would probably be more marked if related to the size or asset value of the cases, becoming less marked in more recent years in the light of the trends noted in 2.3.1 above.

## **2.4 Principal findings arising from administrative receivership responses**

### **2.4.1 Case control considerations for appointing administrative receivers**

Case control considerations including, for example, information and approval arrangements, rather than an assessment that the procedure itself is likely to produce superior financial results, are the most significant determinant in the choice of procedure in favour of administrative receivership. These were seen by insolvency practitioners to be of moderate or greater significance in 69% of administrative receivership cases. Moreover, administration was not considered as a possible alternative to administrative receivership, normally for control reasons, in 52% of administrative receivership appointments.

### **2.4.2 Importance of speed in appointment of office holder**

Our initial work indicated that in 33% of administrative receivership cases avoidance of delay was a significant factor (C or above on a 5 point A to E scale) in the selection of that procedure. This was because assets were considered to be at physical or other

financial risk that may be exacerbated by delay inherent in the more cumbersome administration appointment procedure which pertains under IA 1986.

However, with respect to this subset of 33%, in broadly half the cases (equating to half the assets potentially at risk) had administration under the IA 1986 regime been the only available route, respondents to our follow-up questionnaires indicated that the consequential delay and requirement for an application to the court would not have put realisations at risk.

With respect to the remaining half of the cases, realisations would have been at risk had IA 1986 administration been the only available route. However, in each of these cases the streamlined EA 2002 appointment procedures would have permitted an appointment with a similar timescale and formality as now pertains to the appointment of administrative receivers, and respondents indicated that there would accordingly have been no risk to the realisations.

It is perhaps surprising that some 50% of cases that went the administrative receivership route because speed of appointment was important could equally well have gone the administration route even under IA 1986 procedures. This finding suggests that some of the advantages of administrative receivership may have been overstated in the debate.

Details of response rates, realisations involved and amounts considered to be at risk are given at section 9.3.2 of this paper.

#### **2.4.3 Additional professional costs that would have been incurred had administrative receivership cases gone the administration route**

Comparative cost analysis was sought on cases where there had been no other overriding consideration for choice of procedure. It is not feasible to obtain sufficiently similar pairs of actual cases going the different routes to make precise comparisons between the two IA 1986 regimes and there is of course no factual experience yet of the EA 2002 regime. Accordingly, we sought to ascertain, on a hypothetical basis, how costs of individual cases would have compared had the case

been conducted under each of the alternatives - administrative receivership, administration under the IA 1986 regime and administration under the prospective EA 2002 regime.

Assessment of alternative courses of action and related costs is part of the process of consideration prior to any formal insolvency appointment. Hence a hypothetical exercise of this nature is a valid one, with which practitioners were generally willing and able to help.

Based on the cases reviewed, we estimate that the additional costs of administration under the EA 2002 regime can be expected to reduce total net realisations compared with administrative receivership by just under 1%. (Administration under the IA 1986 regime would reduce comparative net realisations by around 1.5%).

Further analysis of costs, including absolute cost comparisons and the range of reduction in net realisations dependent on case size, is given at section 9.3.3.

#### **2.4.4 Floating charge holders' use of veto over administration**

Resort by floating chargeholders to their veto over administration is quite rare. Appointment of an administrative receiver following the intimation or presentation of a petition occurred in only 2% of administrative receivership appointments. This supports the view that there is in practice often a considerable degree of discussion at an early stage and agreement between the parties involved as to which procedure should be adopted. It is, however, also recognised that the power to appoint an administrative receiver may itself limit consideration of administration in some cases.

#### **2.4.5 Additional powers available to administrators**

Although speed of appointment is an important factor in cases where assets are at risk, respondents indicated that the additional powers available in administration (but not in administrative receivership) in respect of undervalue and preferential transactions would have been of assistance in only 3% of cases. An explanation may be that most cases with a risk of asset dissipation do not involve dishonesty or transactions that can

successfully be challenged. It is also recognised that an administrative receiver may, and on occasion does, arrange for the company to be put into liquidation so that transactions of this nature may be investigated.

#### **2.4.6 New tax consideration arising from the Finance Act 2003**

Discussion of our principal findings with interested parties identified a new factor that will in certain cases move the balance of advantage back toward administrative receivership. Under the provisions of the Finance Act 2003, the appointment of an administrator triggers a new accounting period for tax purposes. That had not been the case heretofore. Appointment of an administrative receiver does not trigger a new accounting period and we are not aware of any proposal to align the tax treatment of the two procedures. Unless the tax treatment of the procedures is aligned, tax mitigation arrangements that have been available both to administrators and administrative receivers will in future only be available to the latter. Having regard to the stated objectives that administration should be the procedure of choice and that administrative receivership be eventually phased out, this difference in tax treatment is a surprising anomaly.

### **2.5 Principal findings arising from administration case responses**

#### **2.5.1 Administration in cases where there is no floating charge.**

41% of administration case responses were in respect of cases where there was no floating charge and where accordingly an administrative receiver could not have been appointed. This indicates that substantial use of the administration procedure has fulfilled an objective of IA1986, to provide a parallel business rescue mechanism to administrative receivership for cases in which there is no floating charge.

#### **2.5.2 Administrations where achievement of a Company Voluntary Arrangement (CVA) was a significant purpose**

In a third of the (63) cases where there was in principle a choice of procedure, a significant purpose of the application for administration was to achieve a CVA. On

the face of it, these cases could only have gone the administration route since the objective of achieving a CVA cannot be achieved on a stand-alone basis in administrative receivership. However, further analysis and supplemental responses on cases that were considered to have CVA potential showed that a CVA had been achieved in only two cases, and remains a possibility in just a further two cases.

Responses indicate that achievement of a CVA is often a secondary or desirable purpose included in the purposes of application (although as a matter of law it should in principle only be so included if likely to be achieved).

The main purpose of our study was to compare insolvency regimes as business rescue vehicles. It does not seek to determine (in response to one of the objectives of the EA 2002) whether there is a substantial number of companies (as opposed to businesses) that are capable of being saved and may be encouraged by early entry into administration. However, the small number of CVAs actually achieved out of this sample suggests that there is a relatively small number of cases that currently go into an insolvency regime where survival of the company is regarded as achievable.

### **2.5.3 Administrations for specific business reasons (“business badged” cases)**

In 49% of cases having a choice of procedure, there were considered to be significant business or operational reasons why the case should have gone and did go the administration route - for example because the nature of certain contacts meant that it was easier to preserve value in administration. In a number of cases where the responses indicated administration (business) badging, there were indications that it would also have been possible to achieve an equivalent result in administrative receivership. In light of the imminent legislative changes that are intended to result in the phasing out of administrative receivership, we did not examine in depth the hypothesis that many of these cases could equally have gone the administrative receivership route. However, the indications that we noted, together with the finding at 2.5.2 above that only a very small number of CVA badged cases actually result in CVAs, may indicate a tendency of proponents of administration in any particular case to overstate the anticipated unique benefits of the procedure.

## **2.6. Overall findings and policy implications**

### **2.6.1 Case for abolition of administrative receivership**

Administrative receivership is difficult to defend from first principles, as it is a private contractual remedy and so liable to eclipse the interests of those who are not parties to the contract. However, a persuasive case for its abolition - evidence that a streamlined administration only regime would enhance business rescue and realisations – has not been made out. It must be questionable whether a reduction in choice of procedure can enhance total welfare (other than the cost savings in the evaluation and selection process arising from an eventual reduction in the choice of procedure). Moreover, the proportion of administrations to total cases has increased markedly in recent years, reaching 50% before the new regime starts to have an impact. This adds force to the argument that abolition of administrative receivership was not necessary or desirable. However, our findings below also suggest that its abolition under EA 2002 should not be materially damaging.

### **2.6.2 Suitability of administration as an alternative procedure**

Our work indicates that in those cases which have gone the administrative receivership route because they required a speedy and simple appointment procedure, there would have been a significant loss of gross realisations - in relation to these cases and in total - if administrative receivership were to have been abolished and administration procedures left substantially unchanged from IA 1986 procedures. However, our work indicates that the simplified administration procedures to be introduced by EA 2002 will avoid the potential loss of realisations. [2].

### **2.6.3 Incremental cost of administration**

The incremental cost of administration over administrative receivership - especially for the larger cases - is moderate in relation to net realisations and unlikely to be a substantial deterrent. Policy makers may regard additional costs of around 1% of net realisations as an acceptable price for a regime of exclusively collective procedures.

#### **2.6.4 EA 2002 administration and number of companies to be rescued**

The purpose of our study has been to compare administration and administrative receivership as business rescue vehicles. Accordingly it was not intended to evaluate the hypothesis that there may be a significant number of companies that are capable of being saved by the introduction of a streamlined and simplified administration regime. Our finding at 2.3.2 indicates that there are relatively few cases that go into formal insolvency proceedings where the company rather than the business is capable of being saved. However, it may be that if administration is considered and used earlier in the distress cycle, more companies could be saved. There is and will continue to be a requirement to confirm actual or prospective insolvency (except where the appointment is by a floating charge holder). This may limit the extent to which the availability of streamlined administration will encourage earlier identification of problems and remedial action.

It would be a useful area for future research to examine what effect EA 2002 has on the number of companies that are saved, and to consider other reforms that might further assist the rescue culture. We are grateful to the Centre for Business Performance practitioner referee for pointing out that other reforms and areas for research might include procedures for facilitating a debtor in possession regime with a “lighter touch” form of administration, and also improved “DIP” (debtor in possession) financing, on which EA 2002 is silent.

### **2.7 Other policy considerations**

#### **2.7.1 Balance of control**

There has been and remains much criticism of the insolvency processes and the control of floating charge holders [3] [13]. The early reform proposals would significantly have reduced the influence of floating charge holders over the proceedings. However, the arrangements enacted by EA 2002 are in many respects very close to those that currently pertain for administrative receivership. Our work suggests that, in terms of preserving welfare measured by realisations, the only

streamlining that might have been essential are the arrangements for simplified and speedy appointment in cases where assets may be at risk [3].

### **2.7.2 Cost and availability of finance**

It was not a purpose of our study to measure the effects on cost and availability of finance of restricting or streamlining insolvency regimes. However, it has not been argued to us, and we have seen no evidence, that EA 2002 will materially affect the cost or availability of finance. Indeed, other recent changes to insolvency law and regimes are likely to be more significant to chargeholders than EA 2002 [4]. While very difficult to measure, the effect of changes in insolvency regimes on cost and availability of finance would be a useful area for study.

### **2.7.3 New ethical and conflict issues**

Extension of the powers of administrators to make distributions may give rise to new conflict and ethical issues requiring consideration. There will be more circumstances in which a practitioner may be engaged in self-review of his work at an earlier stage, rather than handing this on to an independent practitioner who would provide an element of independent review.

The EA 2002 arrangements, giving floating charge holders the power to change the identity of the practitioner to be involved, replace the IA 1986 veto over the procedure of administration. This may by inference suggest that the IA 1986 objective to raise the standards of the entire profession by licensing and regulation have not yet been fully achieved.

**For sections 3 – 10, please refer to the Centre for Business Performance**

**[www.icaew.co.uk/cbp/](http://www.icaew.co.uk/cbp/)**

**Footnotes (references are to the full paper)**

[1] Based on dates of appointment as recorded in company records at Companies House

[2] In none of the sample cases and discussions with those involved in the procedures would the streamlined administration procedures have failed to protect the business or assets at risk.

[3] See also “How the banks won the battle for the Enterprise Bill” - John Willcock, “Recovery” June 2002

[4] For example, the reduction in the effectiveness of charges on book debts consequent on the Privy Council decision in re Brumark [2001 3 WLR 454], and implementation in January 2003 of the small company CVA moratorium provisions of Insolvency Act 2000.

[5] White Paper on Insolvency Law Reform, July 2001 (CMND 5234).

[6] DTI – Enterprise Bill (Insolvency) - Streamlining Administration - July 2002. A summary of the principal changes introduced by EA02 is at given at Appendix 7.

[7] Comparative study of administration and administrative receivership as business rescue vehicles. Preliminary Paper. February 2002. Published on websites of Centre for Business Performance ICAEW and ABRP-R3.

[8] This frequently cited benefit of AR is supported by the finding that 44% of ARs result in going concern sales - Julian Franks and Oren Sussman - The Cycle of Corporate Distress - IFA working paper - April 2000.

[9] The specific purposes are extended but proof of insolvency will remain a requirement for an admin appointment under EA02 except in respect of appointment by a floating charge holder i.e. the practical position will be little changed.

[10] See Appendix 7 for amendments introduced by EA02 - appointments without application to the court

[11] See also appendix 7 re streamlined admin procedures introduced by EA02.

[12] Source [www.insolvency.co.uk](http://www.insolvency.co.uk) . In 2000 there were 429 admins to 1113 ARs = 28% of total. We find at section 9.1 that the proportion of admins has continued to increase markedly reaching 50% of total cases in June 2003].

[13] See, for example, “The Numbers Game” Nick Cohen, Observer 29 June 2003, referring to campaigns by Prem Sikka and Labour MPs Austin Mitchell and Jim Cousins.

[14] See, inter alia, Katz and Mumford - “Should investigating accountants be allowed to become receivers?” - ICAEW April 2000.

[15] As for example in SPI (ABRP - R3) reports and surveys.

[16] In respect of ARs, we have realisations data on 88 = 48% of the cases initially surveyed, based on which we estimate that the sample 182 had gross realisations of £293 million. This in turn implies a market size in terms of total assets involved of over £1.3 billion. (The random sample included two ARs with realisations in excess of £20 million). In respect of admins, realisations data was not generally sought and is limited to 6% of cases originally surveyed, based on which we estimate that the sample 181 had gross realisations of £70 million.

[17] Source – summarisation of data obtained from [www.insolvency.co.uk](http://www.insolvency.co.uk) .

[18] For a study of the cycle, see inter alia Julian Franks and Oren Sussman “The Cycle of Corporate Distress, Rescue and Dissolution” - Institute of Finance and Accounting Working Paper 306 - 2000, April 2000.

[19] This observation ignores the theoretical saving in analysis and selection costs time that may eventually arise from a reduction in choice.

[20] Subject to the taxation anomaly - see 10.6.

[21] See appendix 7. The reserved fund is intended to transfer to unsecured creditors the benefit of abolition of Crown preference that would otherwise benefit floating charge holders. However, while the abolition of Crown preference takes effect from the implementation date, the reserved fund is applicable only to appointments under floating charges created after the implementation date.

[22] For an explanation of the tax issue - see section 9.3.6.

[23] Including but not limited to the issues addressed, inter alia, in the Katz / Mumford research - Receivership following Investigation – ICAEW April 2000.

[24] The failure of EA 02 to assist with DIP (debtor in possession) finance is referred to at section 10.5.