Are 'pre-packs' insolvency proceedings for the purposes of the Insolvency Regulation?

The Proposal for a Directive harmonising certain aspects of insolvency law regulates *pre-packs* and, in doing so, raises some questions about the functioning of private international law rules in relation to them.

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1. Pre-packs in the proposed insolvency directive

The Proposal for a Directive of the European Parliament and the Council harmonising certain aspects of insolvency law (COM/ 2022/ 702 final) contains a series of provisions on *pre-packs* aimed at harmonising the same in all Member States. At present, some legislations, such as the Spanish one, deal with this instrument, while in other States its regulation is based on case law.

The proposal defines a pre-pack as "expedited liquidation proceedings that allow for the sale of the business of the debtor, in whole or in part, as a going-concern to the best bidder, with a view to the liquidation of the assets of the debtor as a result of the established insolvency of the debtor" (Art. 2(p)) and then divides the proceedings into two phases. The first phase, the *preparation phase*, aims at finding an appropriate buyer for the debtor's business or part thereof, while the second phase, the *liquidation phase,* aims at appro-

ving and executing the sale of the debtor's business or part thereof and at distributing the proceeds to the creditors (Art. 19). Thus, the proposal regulates "formal" — insofar as judicial supervision is required —proceedings, which are not limited to sale fitness checks, but also the "court having jurisdiction in pre-pack proceedings shall have exclusive jurisdiction in matters relating to the scope and effects of the sale of the debtor's business or a part thereof in pre-pack proceedings on the debts and liabilities, as referred to in Article 28"(Art. 21).

The preparation phase begins with the appointment by the court, upon request of the debtor, of a monitor who must document and report each step of the sale process; justify why it considers that the sale process is competitive, transparent and fair and meets market standards; recommend the best bidder as the pre-pack acquirer in accordance with Article 30, and state whether it considers that the best bid does not constitute a manifest breach of the best-interest-of-creditors test. In the course of the preparation phase, however, the debtor remains in control of its assets and the day-to-day operation of the business (Art. 22). During this preparation phase, individual enforcement actions may be stayed if the debtor is in a situation of likelihood of insolvency or is insolvent in accordance with national law, in accordance with Articles 6 and 7 of Directive (EU) 2019/1023, where it facilitates the seamless and effective roll-out of the pre-pack proceedings (Art. 23). The monitor shall be heard prior to the decision on the stay of individual enforcement actions.

In the liquidation phase, the court shall, where appropriate, authorise the sale of the debtor's business or part thereof and, if it does not do so, shall continue with the insolvency proceedings. The acquirer shall acquire the business free of debts and liabilities, unless it expressly consents to bear the debts and the liabilities of the business or part thereof.

Along with the above rules, the proposal contains rules concerning criteria to select the best offer (Art. 30); the civil liability of the monitor and of the insolvency practitioner (Art. 31); safeguards in the event that parties closely related to the debtor acquire the business or part thereof (Art. 32); and measures to maximise the value of the debtor's business or part thereof, including steps to obtain interim financing, the exclusion of the possibility of granting payment with priority to bidders or the establishment of limits on the set-off of claims of a secured creditor making an offer (Article 33). In addition, certain provisions are

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included to protect the interests of creditors (right to be heard before the authorisation or execution of the sale, release of security interests in the pre-pack in accordance with the same requirements as those applicable in liquidation proceedings, in both cases with the possibility of certain exceptions (Art. 34) and the impact that competition law proceedings may have on the pre-pack (Art. 35).

2. On the consideration of pre-packs as insolvency proceedings for the purposes of the Recast IR

The proposed directive aims to achieve substantive harmonisation and does not seek to regulate issues of private international law that these proceedings may raise. However, its current wording does raise some questions in this area. One of these concerns its possible inclusion in Regulation (EU) 848/2015 on insolvency proceedings (Recast IR), which has significant implications since, if included, the rules on jurisdiction, applicable law and recognition contained in that text would apply, whereas, if not included, the possible application of general rules, including the Recast Brussels I Regulation, or domestic law rules would have to be considered.

Thus, if subject to the Recast IR, jurisdiction to intervene in these proceedings should be attributed solely to the authorities of the Member State of the debtor's centre of main interests or, where applicable, of the debtor's establishment. These courts shall apply their own law, subject to the exceptions provided for in Articles 5 to 15 of that regulation, and their decisions shall be recognised in the other Member States without any possibility of objection other than on grounds of public policy (Art. 33 of the Recast Brussels I Regulation). Enforcement shall be carried out in accordance with the provisions of the Recast Brussels I Regulation (Art. 32 of the Recast Brussels I Regulation).

In the current situation, the applicability of the pre-pack to the Recast IR depends, on the one hand, on its compatibility with the general rule of Article 1 and, on the other hand, on its inclusion in Annex A of that legal text. At present, Spain has not notified pre-packs as insolvency proceedings, and their fit in the definition in Article 1 may be doubtful with regard to the first phase of the proceedings, which is primarily aimed at finding buyers and is usually conducted confidentially.

Furthermore, the proposed Directive provides an initial response in Article 20 (entitled "Relationship with other Union legal acts"), which states that the "liquidation phase referred to in Article 19, paragraph 1, shall be considered to be an insolvency proceeding as defined in Article 2, point (4), of Regulation (EU) 2015/848. Monitors referred to in Article 22 may be considered to be insolvency practitioners as defined in Article 2, point (5), of Regulation (EU) 2015/848 [...]".

Thus, the intention of the legislator, in keeping the text in its current wording, is to include the liquidation phase of pre-packs in the Recast IR, which does not seem to leave it up to Member States to decide whether or not to communicate them for the purposes of their inclusion in Annex A. A reading *a contrario* of the aforementioned provision leads to the conclusion that the preparation phase does

not, in turn, constitute insolvency proceedings. This could, in turn, mean that it does not in any case or, alternatively, that it is left to the Member States to decide whether or not to include it in the Recast IR. Unless all Member States opt for its inclusion, either possibility leads to divergent solutions being adopted in relation to this preparation phase as regards questions of private international law.

The reasons that led the legislator to make this distinction in the proposed directive can be explained by the usually confidential nature of this first phase, but, from a logical point of view, it is difficult to separate the preparation phase (and the actions that may take place during the same) from the liquidation phase. The continuity between the two phases, if both occur, is undeniable, as demonstrated, for example, by the fact that the monitor will become the insolvency practitioner and the judge will become the insolvency judge.

This continuity seems to lead to the logical conclusion that the jurisdiction to intervene in the preparation phase must be determined in accordance with the Recast IR, because only in this way can we ensure that, once this court has become the insolvency court, the jurisdictional test for hearing the liquidation phase is met. Similarly, the conversion of the monitor into an insolvency practitioner and the requirements that must be met from the outset in anticipation of this circumstance corroborate this reasoning.

From the perspective of recognition, the exclusion of the preparation phase from the scope of application of the Recast IR prevents said phase from benefiting from the automatic system provided for in the Recast IR. It is true that most court actions in the preparation phase will not require recognition outside the State in which they are taken, but it cannot be ruled out that this may be necessary when, for example, a moratorium is granted and a dissenting creditor seeks separate enforcement of its claim in a different Member State.

The application of the Recast Brussels I Regulation does not seem likely in this situation, in the absence of contentious proceedings, which leads to the application of domestic law. At this point, it will be necessary to reclassify the device to determine whether its insolvency rules or the general rules apply to that recognition. In any case, the means of enforcement are likely to be more burdensome and, in any event, the lack of a uniform response will lead to less predictable results.