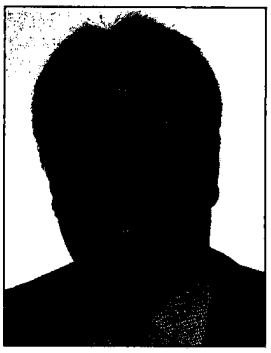
Selling the staff

Charles Wynn-Evans examines the impact of recent decisions on business transfers and insolvency



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'Two Court of Appeal judgments delivered just before Christmas are of considerable importance in terms of clarifying the scope of the potential protections provided by TUPE for affected employees.'

This article discusses two important recent cases that are of considerable importance for those involved in handling transactions that potentially fall within the scope of the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), whether involving an outsourcing or procurement exercise that could attract the application of the legislation either at the commencement or termination of the relevant procurement arrangements. Whether TUPE applies to a particular situation and whether those dismissed around the time of the transfer can claim the protection of the legislation is important for those structuring and documenting the relevant commercial arrangements, in terms of the transfer provisions, and any indemnities, in respect of associated employment liabilities.

Two Court of Appeal judgments delivered just before Christmas are of considerable importance in terms of clarifying the scope of the potential protections provided by TUPE for affected employees and which can be seen as applying an expansive interpretation to the legislation. First, TUPE always applies to transactions out of administration, which otherwise fall within its scope. Second, an employee who is dismissed by administrators prior to a sale can argue that his or her dismissal was transfer-connected and therefore potentially automatically unfair, as well as being a liability for which the ultimate acquirer of the business is responsible, even when there was no particular transaction or purchase in existence or contemplation at the time of dismissal.

Connection with the transfer

The party acquiring a business or taking over a function where the transaction falls within the scope of TUPE (the transferee) will potentially be liable for a dismissal effected prior to the relevant transaction if the dismissal is by reason of or connected with the transfer. A dismissal that is by reason of the transfer is automatically unfair. A dismissal that is for a reason connected with the transfer will be unfair unless it can be shown that there was an 'economic, technical or organisational reason entailing changes in the workforce' (reg 7(1)(b)) (ETOR), which avoids such automatic unfairness and means that the dismissal is tested for fairness on the usual unfair dismissal law principles.

In *Spaceright Europe Ltd v Baillavoine & anor* [2011], the Court of Appeal considered whether, for an individual to be able to claim that his dismissal is connected to the transfer and therefore a dismissal that may be automatically unfair and for which the transferee is liable, the actual transfer, or indeed the identity of the intended transferee, needs to have been identified or be in contemplation at the time of dismissal. This decision resolved the long-standing conflict in the prior Employment Appeal Tribunal case law. In *Ibex Trading Co Ltd v Walton* [1994] it was held that the specific transfer must be contemplated at the time of dismissal if the individual is to be able to bring a claim against the transferee under TUPE. However, in *Harrison Bowden Ltd v Bowden* [1994] it was held that a possible transfer is sufficient to attract the protection of

TUPE in relation to a dismissal rather than a specific transfer to a particular transferee.

In *Spaceright*, the Court of Appeal held that the dismissal of the chief executive officer of the relevant business, on the same day as his employer went into administration, was for a transfer-connected reason and was automatically unfair (even though the business and assets were sold a month later and the identity of the transferee, and indeed the transaction itself, was not in the administrators' contemplation at the time of his dismissal).

The administrators' evidence was that the chief executive's dismissal was decided upon because the company did not need a chief executive after the appointment of the administrators. However, this evidence was rejected and the dismissal was found to be automatically unfair as it was not justified as being for an 'economic, technical or organisational reason entailing changes to the workforce', rather the dismissal was found to have been effected in order to facilitate the sale of the business. The Court of Appeal was satisfied that the dismissal was connected to the transfer on the basis that achieving a sale was the real motivation, not the ongoing conduct of the business. Moreover, as the role of CEO continued to exist post-transfer, the dismissal was not for an ETOR. The ETOR 'defence', as the Court of Appeal put it:

> ... is not available in the case of dismissing an employee to enable the administrators to make the business of the Company a more attractive proposition to prospective transferees of a going concern.

TUPE renders unfair dismissals effected to make a business more saleable.

Saleable business

Those aspects of the decision were matters of fact and provide a useful reminder that TUPE renders unfair dismissals effected to make a business more saleable. The important point of principle affirmed by the Court of Appeal related to the fact that the transferee was liable for the chief executive's dismissal, even though the transferee and relevant transaction were not in the administrators' contemplation when they took the decision to dismiss. The Court of Appeal held that a dismissal can be transfer-related where the identity of the acquirer is not known (or even contemplated) when the dismissal was carried out.

This decision unavoidably increases the risk that acquirers will end up liable for pre-transfer dismissals effected by administrators where it cannot be established that the dismissal truly relates to the

conduct of the business rather than the facilitation of its sale. As the test can be interpreted as being applied effectively retrospectively, the scope for transferees to be liable for pre-transfer dismissals is potentially increased, making all the more important careful due diligence about the reason for pre-transfer dismissals and consequent potential exposure in order to avoid unexpected and potentially significant liabilities.

TUPE and administration

Whether TUPE applies in relation to transactions contemplated or entered into in relation to businesses that have gone into administration is of considerable importance to those structuring, implementing and affected by such transactions. This is particularly the case in the current economic climate in view of the increased prevalence of the use of 'pre-pack' administrations whereby, prior to the relevant business entering administration, a purchaser is identified for the whole or viable part of the business. The commercial attractiveness and viability of transactions out of administration can be affected materially by the extent to which employees and their associated liabilities transfer to the acquirer (transferee) of the business in question.

Following amendments made to TUPE in 2006, the transfer legislation does not apply in its full rigour to 'terminal insolvencies', pursuant to reg 8(7) of TUPE, where:

> ... the transferor is the subject of bankruptcy proceedings or any analogous insolvency proceedings which have been instituted with a view to the liquidation of the assets of the transferor and are under the supervision of the insolvency practitioner.

Then, two important protections provided by TUPE do not apply: the automatic transfer of the contract of employment and associated liabilities of the employees who are in scope for the purposes of the legislation under reg 4, and the rendering automatically unfair of dismissals not capable of justification by way of an ETOR under reg 7. Were administration to fall outside the scope of these protections for employees, there would be obvious potential benefits for acquirers in terms of the actual and potential liabilities which they would inherit as a result of the transaction in question.

There had been conflict in the prior case law as to whether administration constitutes the type of insolvency proceedings, instituted with a view to the liquidation of the assets of the transferor, that falls within the scope of the provisions of reg 8(7). The Employment Appeal Tribunal (EAT) held in *OTG Ltd v Barke & ors* [2011] that administrations (including pre-packs) always fall within the scope of TUPE and cannot fall within the scope of the exemption that applies to, 'bankruptcy... or... analogous insolvency proceedings which have been instituted with a view to the liquidation of the assets of the transferor (reg 8(7))', since (somewhat to oversimplify the EAT's analysis) the purpose of administration is to preserve the business. This contrasted with the earlier EAT decision in *Oakland v Wellswood (Yorkshire) Ltd* [2009], where it was considered that whether a transaction out of administration fell outside the scope of TUPE depended on the 'fact-based' test of the purpose for which the administration was commenced, and whether in reality the insolvency was instituted with a view to the liquidation of the transferor's assets. Doubt had been cast on that view when *Oakland* went to the Court of Appeal, but no specific finding was made on the point.

On 20 December 2011, in *Key2Law (Surrey) LLP v De'Antiquis* [2011], the Court of Appeal resolved this uncertainty, holding that administrations always fall within the scope of TUPE, thereby removing any ability to evade its application based on the precise circumstances in which it was decided that administration was the appropriate form of insolvency into which the relevant business should enter. While many transactions out of administration do entail the purchaser taking on all the employees in any event, this decision does remove the possibility of greater flexibility for purchasers over which employees to take on.

Whether a transaction out of administration fell outside the scope of TUPE depended on the 'fact-based' test of the purpose for which the administration was commenced.

Conclusion

These decisions will not assist those seeking to avoid or limit the exposure to potential liabilities that TUPE creates, reinforcing as they do the width of the protections that TUPE provides for the relevant employees. At least they do (subject to any further appeals) bring certainty to the legal position in relation to the issues that they address. Those considering acquisitions out of administration will need not only to appreciate that TUPE will still apply to such transactions, but also that the possibility that those dismissed by administrators prior to the acquisition may have claims against them needs to be carefully assessed in their commercial considerations. ■

Harrison Bowden Ltd v Bowden [1994] IRLR 564
Ibex Trading Co Ltd v Walton [1994] IRLR 564
Key2Law (Surrey) LLP v De'Antiquis [2011] EWCA Civ 1567
Oakland v Wellswood (Yorkshire) Ltd [2009] IRLR 250
OTG Ltd v Barke & ors [2011] IRLR 272
Spaceright Europe Ltd v Baillavoine & anor [2011] EWCA Civ 1565