SLAUGHTER AND MAY/

Slaughter and May Podcast
Redundancy in focus: The insolvency angle

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<tr><td>Clare Fletcher</td><td>Hello and welcome to the third in our series of Slaughter and May podcasts "Redundancies in focus".

I'm Clare Fletcher, a professional support lawyer in the Employment team, and today I'm joined by Philippa O'Malley and Dave Rintoul, both associates in our Employment team.

Today's episode is called "The insolvency angle". There are five key points that Philippa and Dave will discuss:

1. There key timing issues in the run up to insolvency which businesses need to be aware of

2. Post-appointment handling points of redundancy consultation requirements

3. The discrimination risk faced by administrators

4. The amounts owed to employees in an insolvency/redundancy situation and how/where they can be claimed.

5. Finally, we'll briefly touch on the changes introduced by the Corporate Insolvency and Governance Act 2020.

So Dave, can I ask you to kick us off?</td></tr>
<tr><td>Dave Rintoul</td><td>Yes, so setting the scene - we can see all too readily how the measures put in place to tackle the spread of coronavirus are taking their toll on UK business; added to an already tough economic environment for a number of sectors. Even with ongoing government support and changes to insolvency law, increasing numbers of employers are looking at the prospect of insolvency in the coming months. Which for many will go hand in hand with redundancies.</td></tr>
<tr><td>Philippa O'Malley</td><td>The first point we wanted to cover is the often difficult relationship between on the one hand, the duty to inform and consult in respect of collective redundancies, and the parallel requirement to notify BEIS by filing the HR1 form; and on the other hand, the realities of an insolvency situation.

As a reminder – in a collective redundancy situation, consultation must begin in good time', and in any event at least 30/45 days before the first dismissal. The HR1 form must be filed within the same timeframes.</td></tr>
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	Aside from the impact on employees, a key concern for the employer is likely to be the potential criminal liability that attaches to the failure to file an HR1 with BEIS, for which there is the potential for an unlimited fine and disqualification for directors of up to 15 years.
Dave Rintoul	So not only the company, but also directors and other officers may be liable if the offence was committed with their consent or connivance. So the safest approach would be to file the HR1 as early as possible as a precaution but there will usually be concerns about 'going public' before any decisions have been made about entering insolvency; Steps such as filing an HR1 and starting a consultation can also result in a self-fulfilling prophesy, and might even undermine the prospect of selling the business as a going concern – which could itself cause a breach of the obligations owed to creditors; And the existence of a worked up 'proposal' for the insolvency scenario while continuing to trade as usual could if it strays beyond contingency planning indicate wrongful trading. And if a sale out of administration is genuinely expected (such as in a pre-pack scenario) without any redundancies planned, then the obligation may not necessarily be triggered at that point.
Philippa O'Malley	Due to the criminal liability that can attach to failure to file HR1, we suggest employers adopt a cautious approach - as soon as all options that would not involve redundancies are exhausted, so that there is no real prospect of avoiding the redundancies, the HR1 notification should be filed without any delay. Recognising precisely when that point has been reached at a time of, to quote from the recent Citylink case, 'shock and turmoil' (and when focus may be on rescuing the business) will not be simple, but it's clearly a very important issue indeed.
Dave Rintoul	If there are 'special circumstances' which render it not reasonably practicable for the employer to comply with the notification requirement, the employer could have a partial or complete defence. Insolvency is not of itself a 'special circumstance'- and in any event the employer must still take all reasonable practicable steps to comply with the notification requirements.
Philippa O'Malley	So what might employers do? Don't leave this obligation until the last minute - have your HR1 form 'ready to go' as part of contingency planning. By way of example, working recently with a client on their contingency planning – we planned that as soon the board meeting at which it was resolved to appoint insolvency practitioners had taken place, the HR1 was filed, even though we knew that the insolvency practitioners would be appointed within a matter of hours.

	So we've talked about the pre-appointment period and the difficulties of balancing the timing of collective consultation and the HR1 notification. The next point we wanted to cover is the period after the appointment in the context of 'non-terminal' proceedings.
Dave Rintoul	In relation to post-appointment redundancies (for example, in the context of an administration), it is common for the administrators to put in their own HR1 (even if the company has previously submitted the form). Administrators will be keen to avoid any potential criminal liability for failing to file the HR1, and of course plans may well change and develop once the administrator is appointed. Administrators should still carry out whatever form of consultation is possible, even if that is very limited, to limit the potential exposure in the form of protective awards. The tribunal will usually take into account the impact of insolvency and the surrounding circumstances on the company's ability to consult for the full period.
Philippa O'Malley	In addition, administration will often involve a sale of all or part of the business, so there may be a need to run a TUPE consultation alongside the redundancy consultation. As well as complying with the legal requirements, the fact that there has been some form of consultation, (which could reduce, if not completely mitigate, potential employment liabilities) may make the business more attractive to a potential purchaser.
Dave Rintoul	Now let's look at a particular worry point for administrators relating to potential liability for discrimination claims from redundant employees. The Insolvency Act makes clear that administrators are appointed as individuals, not as firms or a companies. AND that "in exercising [their] functions … the administrator of a company acts as its agent". So, the traditional view is that unless an administrator is acting outside of his functions, there can be no personal liability (because his actions are to be treated as if carried out by the company). However, unlike the bulk of statutory employment liabilities (which are imposed solely on the employer), the Equality Act provides that individual employees and officers can incur liability for unlawful discrimination.
Philippa O'Malley	That means that administrators may potentially become personally liable in one of two scenarios: 1. where the administrator either "knowingly helps" a party to discriminate; or 2. where (in a reversal of the normal statutory position) the administrator is acting as principal in respect of unlawful discrimination by its agent
Dave Rintoul	This is what was argued in a 2011 case, Spencer v Lehman Brothers - which was a case that managed to seriously spook administrators.

	The Claimant was employed by Lehman when it went into administration. The Administrators asked management for recommendations on who to make redundant. The Claimant was on maternity leave and, pursuant to the manager's recommendation, she was made redundant. The Claimant brought a claim in the Employment Tribunal against the administrators for sex discrimination, arguing she was disadvantaged because she was on maternity leave. Although the managers of Lehman made the recommendations, and the company actually effected the redundancies, it was argued that the company was simply acting under authority derived from the administrator.
Philippa O'Malley	Remember the Insolvency Act says that administrators are agents of the company. But it was claimed in Spencer that the administrator could be acting as principal and the company its agent for the purposes of the Equality Act. In the event, Spencer failed on its facts – there was no sex discrimination for which Lehman or the administrators could be liable. However the tribunal endorsed the suggestion that there could have been personal liability as principal, if there had been unlawful discrimination by Lehman.
Dave Rintoul	It's only an employment tribunal decision, so non-binding, but it opens up the possibility that an employee complaining of discriminatory selection for redundancy could successfully claim against an administrator, if in practice that administrator gave authority to company managers to decide on the redundancies.
Philippa O'Malley	Of course the decision doesn't neatly fit with the general position that the administrators act as agents for the company, so it has been met with a lot of scepticism.
Dave Rintoul	That's right but it has caused a lot of stress for administrators since 2011 and clearly no-one wants to be the Guinea Pig – at least we are not aware of it having been tested. So, we have looked at some of the key issues relating to redundancies that exercise employers and insolvency practitioners. For employees who face losing their job, an issue at the forefront of their minds will be what sums owed to them will they be able to recover from the insolvent employer and from the government?
Philippa O'Malley	In terms of the priority of asset distribution on insolvency – generally employment liabilities rank as unsecured claims (and so rank second to last in the order of priority when the business' assets are realised, which in practice means employees would only receive a small fraction of the sums owed to them). Notice pay, redundancy pay, compensation for unfair dismissal and for wrongful dismissal would all be unsecured claims, so the

	employee might only get a few pence in the pound from the insolvent estate for these amounts. However, employees are treated as preferential creditors for some employment liabilities, including capped amounts for remuneration and uncapped holiday pay
Dave Rintoul	And an employee may have a separate claim to the National Insurance Fund for certain guaranteed debts (including certain arrears of pay, holiday pay, unfair dismissal compensation, a statutory redundancy payment etc.). It is also worth noting that employees can claim these amounts from the National Insurance Fund if they transfer from an insolvent business under TUPE. If the National Insurance Fund meets a claim then the employee's claim against the employer for the same amount is extinguished, and the Secretary of State will have a subrogated claim against the employer. Any part of the employee's claims that are not met by the National Insurance Fund, he or she retains the right to claim the balance against the insolvent employer (or, if TUPE applies, the purchaser of the insolvent business).
Philippa O'Malley	Although not strictly related to redundancy, it is also worth noting that, if employment contracts are adopted by the administrator (14 days post-appointment), then certain employee liabilities arising post-administration will become 'super priority' claims, which means they rank higher even than the administrator's fees and expenses (which are normally paid before any other debts). This is likely to be a key concern for administrators and is an example of the conflict between redundancy law (which potentially requires a lengthy consultation period before any dismissal) and insolvency.
Dave Rintoul	Finally we think it is worth briefly mentioning the employment implications of the new standalone moratorium procedure introduced under the Corporate Insolvency and Governance Act 2020, which is intended to allow struggling companies some 'breathing space' from creditor action for up to 40 business days, to help it avoid formal insolvency proceedings.
Philippa O'Malley	In terms of the interaction with employment-related debts, the Act provides for a 'payment holiday' in respect of certain debts owed to employees such as expenses and termination payments. However, most employee costs (including employee wages for the period before or during the moratorium would not be subject to a payment holiday. Further, those debts would be afforded 'super-super' priority, which would mean they would sit above even adopted employee liabilities in the 'waterfall' in the context of an administration or receivership (which have so-called 'super priority').
Clare Fletcher	That brings us to the end of today's podcast – thank you for listening. Do look out for future episodes in this podcasts series, which we will be publishing in the coming weeks. You can find all of our podcasts via the Slaughter and May website. Thank you and goodbye for now.