07 February 2012

Our ref: ICAEW Rep 12/12

Cathryn Law
3rd floor Abbey 1
Department for Business, Innovation and Skills
1 Victoria Street London
SW1H 0ET

By email: tupe.callforevidence@bis.gsi.gov.uk

Dear Ms Law

Effectiveness of transfer of undertakings (protection of employment - TUPE) regulations 2006

ICAEW welcomes the opportunity to comment on the insolvency related aspects of the call for evidence *Effectiveness of transfer of undertakings (protection of employment - TUPE) regulations 2006* published by the Department for Business, Innovation and Skills (BIS) on 23 November 2011, a copy of which is available from this link.

ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 136,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

ICAEW's regulation of its members and affiliates in insolvency is overseen by the Insolvency Service, and ICAEW is the largest of the Recognised Professional Bodies under the Insolvency Act, currently licensing around 700 practitioners. ICAEW's Insolvency Committee is a technical committee made up of Insolvency Practitioners working within large, medium and small practices. The Committee represents the views of ICAEW licence holders.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

Liz Cole
Manager, Company Law, Insolvency & Pensions

T +44 (0)20 7920 8746
E liz.cole@icaew.com

APPENDIX

GENERAL COMMENTS

1. When implemented, the Transfer of Undertakings (Protection of Employment) Regulations 2006 were intended to give insolvency practitioners more opportunity to save businesses and remove the risk that potentially viable businesses would be shut down because purchasers are unwilling to assume the TUPE liabilities associated with them. Unfortunately the legislation did not go nearly far enough to achieve this, and we make some recommendations below regarding points that should be addressed.

Consultation

2. The regulations should be amended to restrict the consultation period following an insolvency event to a maximum period of 14 days (to conform with paragraph 99(5) of Schedule B1 of the Insolvency Act 1986 (as amended) on adoption of contracts of employment). This is because it is unrealistic to expect a consultation period of longer than the period allowed by the Insolvency Act in which to decide whether employment contracts will be adopted or not, as it is often the case that the employer will not have funds available to pay all of the existing employees (including the amounts required for PAYE and National Insurance) for the length of the consultation period. (This should not, of course, alter the position outside an insolvency, where consultation should be commenced in accordance with the current position.)

3. By the end of the 14 day period permitted, the insolvency officeholder will have made initial decisions over which employees are to be kept on and which dismissed, if a sale of some or all of the business is, or may be, achievable. (If no sale is achievable, then everyone will be dismissed and the assets sold on a break-up basis) At that point it is necessary to make those dismissals.

4. When a purchaser makes an offer for a business - unless and until the regulations are amended (see paragraph 7 below) - the price is normally discounted to take into account the likely costs of dealing with and settling TUPE liabilities, including unfair dismissal and/or protective award claims, which might fall on the purchaser. If this discounted offer is less than the price that could be obtained for the assets on a break-up basis, the officeholder will normally be obliged to reject the offer, close the business down and sell the assets piecemeal, thus fulfilling the statutory obligation to obtain the best outcome for creditors. Of course, the business and all the associated jobs will be lost.

5. There should not, in principle, be a penalty (the above reduction in price, which leads to closure being preferable to a going concern sale) for taking the commercial decisions required to preserve **some** employment, which effectively leads to **no** employment. However, decisions on who is dismissed must be justifiable and discrimination on sex, race or age grounds is not acceptable.

6. The commercial decisions that must be taken to produce a saleable entity will almost always involve reducing staff levels, whether by closing down entire divisions of the business or by dismissing some employees in some or all areas. This, combined with other changes to the operations, may reduce the cost base sufficiently to produce a viable business which is attractive to a purchaser.

Unfair dismissal and protective awards

7. The regulations should be amended, consistent with the insolvency exemption in Article 5 of the Directive, to prevent unfair dismissal claims and any protective awards resulting from failure to consult, in either case resulting from the actions taken before/during the insolvency, from passing to any purchaser. This would be the most significant step towards reassuring purchasers that they will not inherit a substantial liability which was not of their making and over which they have no control. In an ordinary solvent situation, a purchaser would be likely to have either sufficient time to ensure

that all consultation obligations have been met, or that a suitable indemnity is available from the seller. Neither is likely to be true on insolvency.

Other liabilities which transfer under TUPE

8. The regulations should be amended consistent with Article 5 of the Directive to prevent other employee liabilities passing to the purchaser for a sale within a formal insolvency process (but length of employment should continue, so that rights are preserved). Set against unfair dismissal, most other amounts are relatively small, but in a labour-intensive business the amounts can be substantial. Furthermore, the purchaser and the Redundancy Fund will have to keep records of transferred employees so that should they subsequently become redundant or be dismissed, the correct amount can be paid from the Redundancy Fund and the correct amount by the then employer.

Practical insolvency considerations

9. On insolvency, often the only way to preserve the employment is to sell the business. Therefore, the *Litster* line of authority and recent decisions which imply that (even if there is no purchaser in view) a redundancy/dismissal may be unfair if a purchase is later consummated should be reversed for a sale within a formal insolvency process. The regulations should be amended to achieve this.

10. We also believe that legislation should be generally understandable by the non-lawyer. Although it is sensible that in any complex case a specialist is involved, for many insolvencies the first point of contact for distressed/confused employees is their union representative or indeed the insolvency officeholder or their staff. It is not helpful if the drafting is so complex that it cannot be understood by these people.

11. Restriction of the insolvency concessions to administration/CVA only would have removed the confusion caused by the difference between the legislation and the Guidance Note. The Guidance Note states that the Regulations apply to collective insolvency proceedings, the Regulations themselves make no such distinction. Given that one of the aims of the Enterprise Act was to promote the use of administrations over administrative receivership, it is surprising that this was not made explicit. It is certainly not clear from the Regulations themselves that administrative receiverships are excluded, albeit that administrative receiverships are increasingly rare.

Information requirements

12. In an insolvency, there should be at least a partial exemption from the information requirements specified in Regulation 11. In an insolvency it is rare for records to be in good order. Of course, the insolvency practitioner should provide everything to the purchaser that they can, but there is no point adding another cost/creditor to dilute already scarce returns when this can be avoided. It would be unhelpful, and of no benefit to the creditors, if the insolvency officeholder were to have to expend time and cost in trying to remedy the failings of the insolvent company with regard to record-keeping.

13. Regulation 12(5) provides for compensation of no less than £500 per transferred employee, so where a business of 100 employees is transferred from an insolvency where the records are poor (very common) then there is a potential cost of £50,000. It is not clear whether this will be an unsecured creditor or an expense of the administration, although it would be unwelcome were it to be an expense.

RESPONSES TO SPECIFIC QUESTIONS/POINTS

Question 13: Should more be done to clarify the application of TUPE in insolvency situations? If so, would this require changes to the legislation, for example, by setting out which insolvency procedures fall under which provisions, or would more detailed guidance than currently provided be sufficient?

14. Yes, we strongly believe that more should be done to clarify the application of TUPE in insolvency situations, and that this will require legislative changes, which should include setting out which insolvency procedures fall under which provisions (rather than guidance, which would not be sufficient).

Question 14: Have the 2006 amendments meant that transferees (ie businesses taking over the contract) have a greater awareness of potential liabilities, and has this helped to reduce transaction costs and risks? If not, how could this be improved?

15. Please see our comments in paragraphs 1 to 13 above.

Question 15: Should liability for pre-transfer obligations be transferred entirely to the transferee as is the case currently in the Regulations ie should the business taking on the contract take on all the liabilities of the business or part of the business they are taking over? Or should both parties be jointly liable, as permitted by the Directive.

16. We believe that, instead of the options given here, the regulations should be amended such that these liabilities remain with the seller where there is a sale within a formal insolvency process, which we believe is permitted under article 5(1) of the Directive, set out below:

> *Unless Member States provide otherwise, Articles 3 and 4 shall not apply to any transfer of an undertaking, business or part of an undertaking or business 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 a competent public authority (which may be an insolvency practitioner authorised by a competent public authority).*