



Financial Recovery

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Collective Redundancies and Meaning of `Establishment` – CJEU Judgment

- The Court of Justice of the European Union has released its judgment in the case of *USDAW and Wilson* on the meaning of `establishment`, overturning the decision of the Employment Appeal Tribunal.

The case arises from the insolvency of Woolworths and Ethel Austin and concerns the meaning of the term `establishment` in Section 188 of the Trade Union and Labour Relations (Consolidation) Act (TULRCA). Section 188 requires an employer to consult where it proposes to dismiss as redundant 20 or more employees at one establishment. TULRCA is derived from Article 1(1)(a) of the European Collective Redundancies Directive (Directive 98/59/EC).

The question, in the contexts of these two retail chains, was whether `establishment` should be taken to refer to a single store, as the Employment Tribunal had held, or to the business as a whole, as the Employment Appeal Tribunal had held.

The CJEU did not provide a succinct description of an `establishment` but instead noted with approval previous decisions which provide indications of factors to take into account in determining whether there is an establishment. For example, an establishment need not have management or legal autonomy but may consist of a distinct entity, having a certain degree of permanence and stability, which is assigned to perform one or more given tasks and which has a workforce, technical means and a certain organisational structure allowing for the accomplishment of those tasks. The court held that where an organisation comprises several units, it is the entity to which the workers made redundant are assigned to carry out their duties that constitutes the `establishment` for the purposes of Article 1(1)(a) of the Directive, and that the relevant provisions should not be interpreted so as to require account to be taken of the total number of redundancies across all the establishments of an undertaking. The EAT had held that the relevant section of TULRCA did not reflect what the Collective Redundancies Directive had intended. The CEU has overturned this ruling and confirmed that UK law does correctly implement the Directive.

The CJEU has referred the matter back to the Court of Appeal which will need to determine, in respect of the facts of these cases, whether applying the guidance provided in earlier cases and approved by the CJEU, each store which has less than 20 employees can be classed as a separate establishment. - R3 Bulletin 110



Validation Orders under Section 127 Insolvency Act 1986

Section 127 of the Insolvency Act 1986 provides that in a winding up by the court, any disposition of a company's property made after the commencement of the winding up (i.e. the time of presentation of the winding-up petition) is void unless the court makes a validation order in relation to the transaction. When considering retrospective validation orders, the court is concerned to balance the interest of the buyer and those of the company's creditors and is more inclined to validate dispositions that were made in good faith, at arm's length terms for proper consideration and before either the company or the buyer became aware of the existence of the winding up petition.

In November 2013, SMC Properties ('SMC') sought to sell a property which had been threatened with repossession by its mortgagee. In February 2014, a petition for the winding up of SMC was presented. SMC sold the property to the buyer in March 2014 and a winding-up order was made a month later. The buyer made a retrospective application for a validation order in relation to the transaction, asserting that it had been made in good faith, at arm's length and had been at a fair market value. The Liquidator argued the sale was at an undervalue and that as such, the transaction should not be validated.

Registrar Briggs said that the purpose of Section 127 was to protect the interests of unsecured creditors by preventing a dissipation of the company's assets, and by maintaining the principle of *pari passu* distribution. Accordingly the operation of the Section will come into play equally if –

- full value was provided for an asset after a petition is presented in circumstances where the directors pay one of many creditors in full (breaching the *pari passu* principle) and
- a substantial undervalue was provided to a company in the same situation but the directors decided to ensure that every creditor in the same class was paid *pari passu*.

When considering an application for validation the court had to distinguish between the engagement of the section and its effects. The court exercising its discretion, mindful of the policy behind the section, carries out a balancing exercise weighing the interests of the general body of creditors against the target transaction under scrutiny. The principles were summarised in the case of *Denney v John Hudson & Co Ltd* [1992] BCLC 901. They are:

- The discretion is entirely at large. It is not confined by any express statutory requirements.
- The policy is not of invariable application. There are cases where it may be beneficial for the company and the unsecured creditors that dispositions made during the closing period should be permitted to be made so that a company can continue the business in its ordinary course.



- In deciding whether to make a validating order in such a case, the court should endeavour to ensure that the interests of the unsecured creditors are not prejudiced.
- Whether it is desirable that the company should be enabled to carry on its business involves speculation. The court has to carry out a balancing exercise. It should not, save in special circumstances, validate any transaction or transactions where the result might be that one or more pre-liquidation creditors get paid in full at the expense of other creditors, who will only receive a dividend, unless there are special circumstances making such a course in the best interests of the creditors generally.
- A good example might be where goods supplied before the presentation of the petition, which are essential for the company to continue in business, have not yet been paid for. The court might exercise its discretion to validate payment made after the petition was presented.
- A disposition made in good faith in the ordinary course of business at a time when the parties were unaware that a winding-up petition had been presented, normally will be validated unless there are grounds for supposing that the payment was intended to prefer the recipient above other unsecured creditors.
- Good faith alone is not enough. It is a powerful factor in favour of validation, but it must be weighed against the consequences of validating the payment and the extent to which validation would contradict the principle of pari passu distribution.
- In considering whether a validating order is likely to be beneficial to the creditors of the company, Harman J emphasised in *Re Fairway Graphics Ltd* [1991] BCLC 468 that the court will have regard to the interests of all of the creditors and not just certain creditors who may be supporting the winding-up petition to be willing to consent to the application under Section 127.

In the present case the Registrar found that SMC had entered into the transaction in good faith. He concluded that the court would be slow to validate a transaction if there was a significant reduction in the value of the company's assets available to unsecured creditors as a result of it. The Liquidators had adduced evidence that the property was worth approximately £900,000 (although the evidence took no account of the limited marketing period and increased sale costs arising in a distressed sale scenario). The purchaser had paid £850,000 for the property. The Court applied a 5% margin of error to the Liquidators' valuation of £900,000 and ruled that, given the minimal difference between the Liquidators' valuation and the purchase price paid, creditors had not suffered significantly or at all. Accordingly the court exercised its discretion to validate the transaction. – R3

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This newsletter is for general information only and is not intended to be treated as advice to any specific person. It is recommended that appropriate professional legal advice is sought before acting or relying on any information contained in this publication.

SERVICES WE CAN PROVIDE

Administration:

Usually instigated by the Directors or the bank, and used to provide protection whilst a solution is found.

Company Voluntary Arrangement:

Useful where a company has accrued aged debt which it is unable to service, but is profitable moving forward. An offer is then made to creditors for settlement based on affordability (requires 75% of creditors voting to vote in favour).

Liquidation of solvent or insolvent companies:

Results in the formal closure of the business entity
-solvent liquidations often provide tax advantages

Re-finance:

Seek new funding via bankers and private investors.

Individual or Partnership Voluntary Arrangements:

An alternative to bankruptcy, which allows individuals to offer to repay what they can afford to creditors and freeze the aged debt (requires 75% of creditors voting to vote in favour).

Bankruptcy advice:

The options available and implications of bankruptcy on the individual.

REGAIN CONTROL, SECURE THE FUTURE

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