

# Briefing Note: Buying an Insolvent Business - TUPE and other Employment Issues

## Introduction

This Briefing Note should be read by anyone who is considering buying an insolvent business as a going concern from an insolvency practitioner, including buying the assets of an insolvent business. It may also be a useful point of reference for insolvency practitioners. It only deals with the modifications that apply to TUPE in those circumstances and therefore should be read in conjunction with the latest version of our Briefing Note on TUPE which can be found [here](#) on our website.

This Briefing Note is intended to be an introductory guide and should not be relied upon in place of professional legal advice.

Our Briefing Note on TUPE explains the background to TUPE, when it applies and its effect on regular transactions. In order to assist with the rescue of failing businesses, the Government introduced into the Regulations specific insolvency provisions which allow the purchasers of insolvent businesses to enjoy the benefit of certain exemptions to the general TUPE principles.

## When do these exemptions apply?

Some of the normal TUPE principles are modified when:

- the seller is subject to insolvency proceedings; AND
- an Insolvency Practitioner has already been formally appointed at the time of the purchase.

The fact that a business is in financial difficulty and may have taken advice from an Insolvency Practitioner is not enough. The extent to which TUPE is modified in an insolvency situation, depends on whether the seller is subject to “relevant insolvency proceedings” (*Reg 8(6)*) or “bankruptcy or an analogous insolvency proceedings” (*Reg 8(7)*).

## What are “relevant insolvency proceedings”?

These are proceedings which are under the supervision of an Insolvency Practitioner but not with a view to the liquidation of the assets of the seller. According to guidance from the Secretary of State, this definition is likely to encompass administration, administrative receivership and voluntary arrangements, in other words non-terminal insolvency procedures.

## What are “bankruptcy or analogous insolvency proceedings”?

These arise when proceedings are instituted under the supervision of an Insolvency Practitioner, with a view to the liquidation of the assets of the seller. According to guidance from the Secretary of State, this is likely to encompass compulsory liquidation and creditors’ voluntary liquidation, in other words terminal insolvency procedures.

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#### Summary:

An outline of the modified employment rights and obligations which arise on the purchase of an insolvent business. This guide is to be read in conjunction with our Briefing Note: TUPE.

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### What is the position on “pre-packs”?

A “pre-pack” is a form of administration where the asset sale is virtually agreed shortly before an administrator is formally appointed. The categorisation of a pre-pack as “relevant insolvency proceedings” was thrown into some doubt by a decision of the Employment Appeal Tribunal in 2009 (*Oakland v Wellswood (Yorkshire) Ltd*) which concluded that where administrators had been appointed with a view to ultimately liquidating the assets of the business, the administration could be regarded as bankruptcy or analogous insolvency proceedings. This was never regarded as good law by employment lawyers and the situation has now been clarified by another decision of the Employment Appeal Tribunal (*OTG v Barke*) which suggests that administration, including pre-packs, will always be regarded as relevant insolvency proceedings under Reg 8(6).

### What is the effect of the seller being subject to “relevant insolvency proceedings”?

In this first scenario, the buyer will not be liable for certain pre-existing debts owed to transferring employees or to those employees that would have transferred had TUPE been complied with. The pre-existing debts that do not transfer to the buyer are those debts guaranteed to be paid by the National Insurance Fund and include the following:-

- Up to 8 weeks arrears of pay (subject to the current maximum statutory limit) less basic rate tax and national insurance contributions;
- Up to 6 weeks holiday pay which accrued in the 12 month period prior to the date of the insolvency, (subject to the current maximum statutory limit) less basic rate tax and national insurance contributions;
- Statutory notice pay (subject to the current maximum statutory limit) less notional basic rate tax;
- The basic award in relation to unfair dismissal compensation;
- Statutory redundancy payment

The above limits apply to each relevant employee. It is important to note that the buyer remains liable for those debts owed to employees which are not covered by the National Insurance Fund or exceed the statutory limits set out above. Furthermore, the Secretary of State has no liability for debts arising after the transfer itself.

In addition, the circumstances in which the buyer of a business, subject to relevant insolvency proceedings, can vary the contractual terms of the transferring employees are significantly relaxed under *Regulation 9*. This allows for “permitted variations” to be agreed with appropriate representatives of the transferring employees where the variations are designed to safeguard employment opportunities by ensuring the survival of the business, or the part of the business that is subject to the transfer. This is quite a high evidential hurdle to overcome and the employer who wishes to make changes in these circumstances should have clear evidence to show that the survival of the business is dependent on the need to make changes. The contractual changes can be made after the transfer itself or in advance of the transfer by the seller or the Insolvency Practitioner at the request of the buyer.

Significantly, no changes can be made under Regulation 9 unless the appointed representatives of the affected employees agree. Assuming the appointed representatives agree, then the permitted variation will take effect as a collectively agreed term regardless of whether any individual employee objects to the change. Regulation 9 operates as a statutory right to vary a contract without an employee’s agreement in these limited circumstances.

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### **What is the effect of the seller being subject to “bankruptcy or analogous insolvency proceedings”?**

In this second scenario, some of the most fundamental TUPE protections for employees are removed altogether in order to facilitate the purchase by the buyer.

The automatic transfer principle does not apply and therefore the seller's employees will not automatically transfer to the buyer. As a result the buyer may cherry-pick which, if any, employees it would like to employ following the purchase of the business. However, any employees that are kept on will retain their continuity of employment.

The protection given to employees in relation to TUPE related dismissals, also does not apply. Therefore, any dismissals by the buyer because of the transfer, or for a reason connected with it, will not be regarded as automatically unfair. Furthermore, any existing employment related debts or liabilities will not transfer to the buyer.

Finally, the buyer will be free to employ any or all of the seller's former employees on entirely different terms in accordance with normal contractual principles, save that the employees will retain their continuity of employment.

### **Duty to inform and consult**

Both the seller and the buyer are obliged to comply with their obligations under TUPE to provide information to and consult with affected employees. The requirement to inform and consult and provide employee liability information applies irrespective of whether the business being transferred is solvent or insolvent and, in the latter case, irrespective of the type of insolvency proceedings. While liability for failure to inform and consult is joint and several as between seller and buyer, the reality is that liability is likely to fall entirely upon the purchaser as the seller is insolvent and therefore unable to meet any such liability. In such cases, the buyer and seller should undertake a joint information and consultation process prior to completion in order to minimise any potential risk of liability for failure to inform and consult.

### **Protecting the buyer**

In contrast to a business sale by a solvent company, the asset purchase agreement will invariably be prepared by either the seller's or the Insolvency Practitioner's lawyers and the buyer will be expected to assume all commercial risk inherent in the transaction. It is rare for the asset purchase agreement to contain warranties and indemnities in favour of the buyer in contrast to the usual situation where the parties commonly divide liabilities by means of pre and post completion employment indemnities. Any warranties that are provided by the seller are likely to be worthless in any event in view of the seller's insolvency and such liabilities as arise would rank as unsecured claims and have little commercial value. In such a scenario, there is no substitute for undertaking a thorough due diligence exercise although this can be impractical having regard to the timescales often involved in such transactions and the limited information available to the Insolvency Practitioner and his staff.

At Gaby Hardwicke, lawyers in our Commercial Department have extensive experience of advising all parties, including Insolvency Practitioners in such transactions, and we are happy to partner you through all the stages of the transaction and beyond.

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