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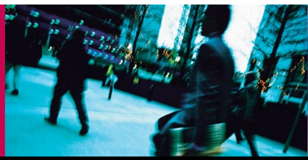

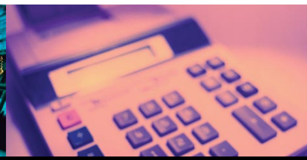

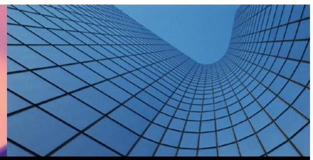

Corporate Recovery Alert

Halliwells' Electronic Alert from the Corporate Recovery Group

Protective Awards are Provable Debts in Liquidation

On 11 June 2008 the Court of Appeal decided that a protective award is a debt which is provable in a liquidation. In a case involving an appeal by the former employees of Compound Sections Limited (in liquidation), an earlier decision of the High Court has been reversed.

Protective Awards

A protective award is an award made to employees by an industrial tribunal where their employer has failed to carry out its statutory obligation to consult employees before making redundancies. 30 days' consultation is required where more than 20 people are made redundant; this rises to 90 days where more than 100 people are involved.

Protective awards are intended to punish employers who fail to consult: they are not simply intended to compensate employees for a loss they suffer and so it is no defence to say that consultation would not have served a useful purpose.

The Decision of the Court of Appeal

The Court of Appeal has decided that a protective award made pursuant to section 189 of The Trade Union & Labour Relations (Consolidation) Act 1992 gives rise to a contingent debt within the meaning of rule 13.12(1)(b) of the Insolvency Rules 1986. That is to say a protective award constitutes a debt or liability to which a company becomes subject after the date on which it goes into liquidation, by reason of an obligation incurred before that date (namely the obligation to consult). The decision will similarly apply in an administration.

The Court of Appeal distinguished its previous decisions in the case of Steele -v- Birmingham City Council [2005] EWCA Civ 1824 and Glenister -v- Rowe [2000] Ch 76 which were both bankruptcy cases and related to debts which were dependant on the exercise of the court's discretion not a statutory obligation.

Practical Implications

This decision has practical implications for the directors of companies in difficulty and for insolvency practitioners. Failure to consult is likely to lead to an increase in unsecured claims. Protective awards can be up to 90 days' pay for the employees concerned and the tribunal's starting point is usually the maximum award.

Directors who do not begin consultation when they have the opportunity to do so might, in theory, be subject to a wrongful trading claim for the amount of the protective award. An insolvency practitioner who ignores the duty to consult could be criticised by creditors if their dividend is reduced by the additional claims of employees.

Consultation is not always feasible. A business in difficulties may be unable to discuss these difficulties openly with the workforce and hope to survive and an insolvency practitioner may be unable to wait to consult before making people redundant. The tribunal can take this into account in exercising its discretion to make a protective award and even if the tribunal cannot be persuaded to do this, the directors or the insolvency practitioner could not legitimately be criticised if consultation was not practical.

The Redundancy Fund will now pay out when a protective award is made and will be subrogated to the employees' claim in the insolvency, part of which will be preferential.

For assistance on this, or any other matter, please speak to your usual Halliwells' contact or Joanne Culley at joanne.culley@halliwells.com Tel: 0161 618 4775.

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