IRISH CONGRESS OF TRADE UNIONS

PROPOSALS FOR THE PROTECTION OF EMPLOYEES IN INSOLVENCY

October 2020

Proposal for the Protection of Employees in Insolvency

1. Introduction

The following document is written in response to the questions posed by the Tánaiste in his letter to the chair of the Company Law Review Group (CLRG).

In the process we seek to address the general silence in company law on the position of employees, who, despite this, are more than any other actors, crucial to the life and success of companies, are most dependent on their employer companies for their living and existence and who are the most vulnerable in corporate insolvency.

The question of the inadequacy of the protection of employees in insolvency was most recently considered in the following reports, commissioned by the then Coalition government in the wake of the Clery's liquidation in 2015:

(i) "Expert Report and Review of Laws on the Protection of Employee Interests when Assets are separated from the Operating Entity. - Report to the Minister for Jobs, Enterprise and Innovation and the Minister for Business and Employment. - Nessa Cahill BL & Kevin Duffy, Chairman of the Labour Court - 11th of March 2016." (Duffy/Cahill Report)

(ii) "Report on the Protection of Employees & Unsecured Creditors – Company Law Review Group – June 2017" (CLRG 2017 Report)

The former report dealt with Employment Law aspects of the problem while the latter examined the adequacy of protection for employees from the Company Law point of view.

Both made a series of separate recommendations, all of which, nearly five years later in the case of Duffy/Cahill, still await implementation and the clear position of ICTU is that both reports and their recommendations should be implemented without further delay.

The recommendations of both reports have to do with many current issues facing workers, most of which are reasonably foreseeable, some bearing a remarkable resemblance in part or in whole to the Clery's debacle, such as in the case of Debenhams. . Equally importantly, while the present government's renewed focus on protections for employees, deriving as it does from the Programme for Government is, of course, welcome, its credibility will be immeasurably enhanced by delivery on existing recommendations in this area.

In short, offering to examine protections for workers in insolvency cannot just be a political" photo-opportunity", "tick the box" exercise or "get out of jail "card for the government. It has to be backed up by action and robust measures.

A good way to start is by implementing existing reports and demonstrating an understanding that this is not a problem for which the trade union movement alone has to produce the answer. Rather both the Department and the CLRG have to demonstrate this is a shared problem and obligation, a view which we are confident is shared by much of the public.

2. "Review whether the legal provisions surrounding the liquidation of companies effectively protect the rights of workers"

A. Company Law and Employees

S 224 Directors duties to Employees

The provisions of section 224 of the Companies Act 2014 read as follows:-

"(1) The matters to which the directors of a company are to have regard in the performance of their functions shall include the interests of the company's employees in general, as well as the interests of its members.

(2)Accordingly, the duty imposed by this section on the directors shall be owed by them to the company (and the company alone) and shall be enforceable in the same way as any other fiduciary duty owed to a company by its directors."

The provision recites those of the previous 1990 Companies (Amendment) Act section 52 , which in turn was based on similar provisions in section 309 of the then UK Company (Consolidation) Act 1985.

Its intent was to impose a significant and distinct statutory duty on directors with regard to their employees in general (and also members of companies).

However, despite its undoubted intentions, the provisions of subsection (1), and therefore the purpose of the whole section, is completely neutralised by the second subsection in that its beneficiaries, i.e. employees and members may not themselves enforce or vindicate their rights.

Accordingly the ICTU is putting forward two proposals:-

ICTU Proposal 1

Amend S 244 by replacing the existing sub section 2 with a new subsection 2 as follows:-

"Accordingly, the duty imposed by this section on the directors shall be enforceable directly by employees, by members of the company or by an authorised officer on their behalf."

Effect of Amendment
The effect of such amendment would to allow for direct vindication of rights under s 224 by employees without having to depend on others, such as an "altruistic liquidator "in the case of employees as suggested by one legal commentator.

Further considerations
A further consideration in this connection is the extension of this duty to the directors of holding or parent companies, whose acts and omissions can have a very significant impact on the employees and members of subsidiaries. In such circumstances it seems entirely just and reasonable to impose such a duty through the "corporate veil".

In this regard and in order to underline the importance of this provision in the Companies Act and to re-inforce the intentions of the Oireachtas to emphasise directors duties in this regard, all directors should sign an undertaking on assuming office, acknowledging their duty under section 224 (as amended and reinforced).

ICTU Proposal 2

Add a new sub section (3)

"The statement by a director referred to in s 233 (3)of this Act shall include a specific acknowledgement of their duty to have regard to the interests of the company's employees in general, as well as the interests of its members in accordance with this section."

Effect
The effect of this further amendment would be to reinforce directors' obligations and compliance in this regard in the statutory statement which accompanies their consent under S 223 at the commencement of their directorship.

The breach of their statutory duty under section 224 by directors (including shadow directors) should leave them open to serious penalisation at the level of a category 1 or 2 offence, including disqualification for a minimum period of 5 years, apart from any other legal or other proceedings which may arise from such a breach. This is in order to provide for a penalty which is sufficiently dissuasive and to match the importance and distinctiveness of this statutory duty legislated for by the Oireachtas.

S 225 Directors Compliance Statements (DCS)

DSC's were originally proposed by a group examining the accountancy and auditing professions which was chaired by the former Senator Joe O'Toole and which was established in 1999 following the Dáil Public Accounts hearings on DIRT . Among the group's recommendations was one for annual compliance statements by directors, acknowledging their responsibility for securing the companies compliance with its relevant obligations under statute. The group saw this as a very effective mechanism for achieving corporate compliance.

Following their report in 2000, their recommendation for statutory DCS's was given force by S45 of the Company (Auditing & Accounting) Act 2003.
However, the then Minister of State for Trade & Commerce at the Department of Industry & Commerce , who was also of the view that it was an effective corporate compliance mechanism , referred the section to the CLRG in order to examine its " proportionality , efficacy and appropriateness".
Despite the opposition of the three largest public interest groups on the CLRG – ICTU, ODCE & Revenue, the original proposed measure was significantly watered down to apply only to a small cohort of large companies (balance sheet total of € 12, 500, 000 and annual turnover of € 25,000,000, and with a severely limited range of compliance obligations (mainly tax matters) .

Congress's view is that the current provisions for DCS 'sunder section 225 do not go far enough in terms of their reach or content but notes that further consideration of DCS's is scheduled for the current CLRG work programme.

In the interim, however, provision should be made in the case of directors' statutory duties for compliance with employment rights and with the obligations of directors to employees under section 224 (as amended above).
Accordingly, the ICTU makes two proposals to amend this section.

ICTU Proposal 1

Amend S225 (1) to include a two new sub sections on employment law, company law and employee interests with regard to compliance with s244 as follows:

"(c) Employment Law
"employment law " means –
(a) Employment Law statutes
(b) Employment rights of employees whether express or implied in the contract of employment whether by collective agreement or otherwise.
(d) Employee interests
"employee interests " means
Employee interests generally and compliance with the provisions of S 244 of this Act
(e) Company Law

"Company law" means –
The provisions of this Act with regard to employees

ICTU Proposal 2

Remove sub sections (7) & (8) to make the section (as amended by the ICTU interim proposal) applicable to all companies, without exemption.

Effect
The effect of both proposals will be to make it a general compliance requirement for all directors of all companies to reflect the original purpose of DCS's as a corporate compliance mechanism, especially with regard to employees, and to achieve a similar universal reach as for example statutory Health and Safety provisions.

S 682 Liquidator to report on conduct of directors
One of recommendations of the CLRG 2017 report referred to above is the inclusion of a new question on the liquidators S 682 Report to the ODCE to specifically address the consideration given to employees by the directors of the company in the period immediately prior to liquidation . This obligation should be enhanced by specific reference to compliance by directors to their obligations under S 224 & 225 of the Companies Act.

ICTU Proposal

Amend S 682 to include new subsection (3) as follows:-

"Such report shall include specific reference to
(i) The consideration given to employees by the directors of the company in the period prior to liquidation
(ii) Compliance by the directors with their obligations under s224 of this Act
(iii) Compliance by the directors with their obligations under s 225 of this act

Effect
The effect of this will be to enhance compliance by directors and companies with regard to the rights and interests of employees generally and specifically in the period prior to liquidation, the breach of which may leave them open to action by the ODCE.

S 819 Declaration by court restricting director of insolvent company in being appointed or acting as director etc.

This section provides for the restriction of directors of insolvent companies for up to 5 years.

However, the court should have discretionary power to make a declaration for lengthier more dissuasive periods of disqualification in more serious cases of abuse, particularly of the interests of employees, with a minimum period of disqualification of 5 years.

In this connection, the non-compliance of directors with their statutory duty to have regard to the interests of employees (see above) should be specifically included in the criteria for declaration by the court.

ICTU Proposal

Amend section 819 (1) as follows (underlined):-

(1) "On the application of a person referred to in section 820 (1) and subject to subsection (2) , the court shall declare that a person who was director of an insolvent company shall not , for a period of 5 years , or such further period as the court decides as just and equitable in the circumstances …… "

Amend section 819 (2)(a) as follows (underlined):-

"The court shall make a declaration under subsection (1) unless it is satisfied that –

(a) The person concerned has acted honestly and responsibly in relation to the conduct of the affairs of the company in question, whether before or after it became and insolvent company.

(b) And the person concerned has fully complied with their obligations with regard to the rights and interests of employees generally, under employment law, their contracts of employment, collective agreements, this Act or generally. "

Effect

The effect of these amendments should be to enhance compliance with directors' obligations, including those concerning employees, through more dissuasive measures.

B. The Liquidation Process

S 571:-Petition for winding up and appointment of provisional liquidator and the powers of the court.

There are reports from Congress affiliates canvassed that invariably employees are not put on notice of the intention to petition the court by the company, by other creditors or by contributors or contributories of the company, so that the first that employees learn of the situation is after the petition is granted and the provisional liquidator(s) appointed.

While it is acknowledged that a primary function of a provisional liquidator is to secure the assets of the company, nevertheless ,it has to be equally acknowledged that more than any other creditor, employees are generally totally dependent on their employment for most aspects of their income, livelihood and, indeed ,existence.
Given this vulnerability they are therefore entitled to be put on notice of any such application with the right to be heard by the court and so that and the court can take account of any representations they may make as well as of the consideration given by the directors to the employees in the period immediately prior to liquidation, including directors duties to employees under S224.of the Act of 2014.

ICTU Proposal

Amend s 571 as follows (underlined):-
The court shall not give a hearing to a winding –up petition unless:

(i) **prima facie case for winding up has been established to the satisfaction of the court**

(ii) **<u>employee creditors have been put on notice of such a petition and have the opportunity to be heard by the court in respect of such a petition</u>**

(iii) **<u>the court has received full details with regard to the employees and their rights , entitlements and interests including any enhanced redundancy terms.</u>**

Effect
The effect of this proposal would be to prevent a petition being heard without employees knowing about it or having an opportunity to be heard on any matter of concern to them, including the opportunity to argue for an alternative avenue such as Examinership or Rescue. It would also ensure that the court would be aware to the maximum extent of employees' rights and entitlements, including the regard had by directors and the company to employee interests under s224 & 225 (as amended) as well as the existent of any enhanced terms of redundancy in the event of liquidation

<u>S 621 – Preferential payments on winding up</u>
The present section 621 at sub section (2) (b) gives preference to "all wages or salary" as defined sub section. This is in addition to any other enactment providing for priority of a particular debt or sum in a winding up. Such enactments are those covered by S 49 & Schedule 5 of the Workplace Relations Act 2015.

However a problem has arisen with, for example, terms expressly or impliedly incorporated into the employee contract by collective agreement or by award of the Labour Court, such as enhanced redundancy terms.

Accordingly is it necessary to provide for such eventualities by amendment of S 621.

ICTU Proposal

Amend s 621 (2) (b) by the addition of a new sub sub section as follows (h) " Any award made by the Labour Court pursuant to the Industrial Relations Acts 1946-2015 with regard to entitlements in the employment contract , whether express or implied by collective agreement or otherwise.

Effect
The effect of this amendment would be to allow such awards to be afforded priority as a sum or debt in a winding up.

S 627 Powers of liquidator
An issue has arisen in at least one liquidation, where the liquidators raised questions about their" locus standi" before the Labour Court in a referral by employees under the Industrial Relations Acts.
In a separate liquidation the DSP asserted, apparently on advice from the AG, that the liquidator is not an employer for the purposes of the Protection of Employment Act 1977.

However, S627 of the Companies Act 2014 lays out the powers of the liquidator which include in the accompanying table at (1) (b) the power to "defend any action or other legal proceeding in the name and on behalf of the company".

Therefore any uncertainly about the obligations of the liquidator with regard to employee claims and complaints and referrals to the WRC & the Labour Court should be removed.

ICTU Proposal

Table 1 (b) to be amended as follows:

"defend any action or other legal proceeding in the name and on behalf of the company , including in the name and on behalf of the employer in proceedings and referrals concerning employee disputes and complaints before the Workplace Relations Commission and the Labour Court

Effect
The effect of this amendment would be to provide clarity on the role of liquidators in proceedings before the WRC including the Labour Court, which , in accordance with the terms of S 678 of the Companies Act 2014 are exempt from any stay on proceedings.

S666Appointment of committee of inspection in a court ordered winding up

Given the extent of their interest in the company, employees should, as of right, and in the interest of maximum transparency, be entitled to be represented on any committee of inspection should they so elect.

ICTU Proposal

Accordingly section 666 (1) should be amended as follows by the inclusion of a new sub section as follows:

"(c) provided always that where a committee of inspection is appointed it shall include not less than one employee creditor member to represent employees creditors, should they so elect"

Effect
The effect of this amendment will be to allow employees to be represented as of right , should they wish to , without prejudice to any other rights they may have under employment law, contract or collective agreement and without interference with the rights of other creditors.

A similar amendment should be made to section 667 – Appointment of committee of inspection in a creditors' voluntary winding up.

C. Informal Insolvency

The CLRG's report of 2017 made three recommendations with regard to or connected to the problem of "informal insolvencies" or "walkaways".

One recommendation proposed legislative change for access to the SIF for employees whose employer has not entered into formal insolvency .Another proposed consideration of a Self-Administered Liquidation scheme for small companies with relatively minor amounts of debt .Yet another recommended that directors of insolvent companies who fail to arrange for the appointment of a liquidator to be automatically deemed to be restricted in accordance with S 819.

None have been actioned to date, despite the fact that it is well recognised that employees and other vulnerable creditors can be left in an intolerable "limbo", and, most importantly in the case of employees, prevented from access to the SIF.

Accordingly the lack of resolution on the question of informal insolvencies warrants further serious discussion to see if there are additional measures that could be examined and which could assist in resolution of this long standing problem, including imposing personal liability on directors of such companies or providing for disqualification in certain circumstances.

ICTU Proposal

If consideration is being given to a Self-Administered scheme for small companies, there is merit in revisiting the question of an equally simplified and less costly petition procedure for employees in particular to enforce the formal liquidation of such companies so that they, the employees are able to qualify for payments under the SIF as provided for in the Act of 1984.

Effect
The effect of any such change or amendment would be to significantly reduce the burden of cost and therefore risk for employees (and unsecured creditors) in placing insolvent unliquidated companies into a formal insolvency procedure so that they, the employees, can qualify for payments from the SIF under the Protection of Employees (Employers Insolvency) Act 1984 (if it not amended to include informal insolvencies.)

3. Review the Companies Act with a view to addressing the practice of trading entities splitting their operations between trading and property with the result being the trading business (including jobs) go into insolvency and assets are taken out of the original business.

This question was examined in some detail in Duffy/Cahill from the point of view of Employment Law and the impact on employees and also with regard to relevant provisions within the Companies Act 2014.Specifically the report had regard to the following sections: 599 (Contribution Orders), 600 (Pooling Orders), 604 (Unfair preference), 608 (Return of assets which have been improperly transferred), 610 (Civil liability for fraudulent or reckless trading) , 612(Power of the court to assess damages against certain people) & 621 (see above).

Sections 599, 600 & 608 were also considered by the CLRG in formulating their 2017 report.

However there is understood to be a view at a high level that sections 599 and 608 are underutilised, which of itself , along with the re-posing of the question of separation of assets as above , clearly merits revisiting this aspect of company law. Further, it is nearly 7 years now since the Act was passed, heading for 5 years since the Duffy/Cahill report and well over 3 years since the CLRG report.

S 599 Related company may be required to contribute to the debts of company being wound up

A related company is defined by section 2 (10) of the Companies Act 2014 as , inter alia, a holding company or subsidiary , subject to the conditions laid down in the section.

Section 599 repeats the provisions of section 140 of the Companies Act 1990. The original Head of the Bill for the 1990 Act replicated in total the provisions of section 30 of the New Zealand Companies Amendment Act 1980 (now section 271(a) of the (NZ)Companies Act 1993).

That section of the New Zealand Act provides that holding companies or subsidiaries or other related companies can be ordered to contribute to the debts of a related insolvent company.

However, as the CLRG 2017 report notes "… due to political concerns at the time that the provisions were **"anti-business" , a number of changes were made in the drafting process to increase the onus of proof for any party seeking a contribution order"(** CLRG Report 2017 Ch. 3.2.2)

Therefore ,unlike the equivalent New Zealand statute, the Irish version contains a much higher threshold of proof in that it states in sub section 2(5):-

"No order shall be made under this section unless the court is satisfied that the circumstances that gave rise to the winding up of the company are attributable to the acts or omissions of the related company"

This represents an express prohibition on making an order, above all other considerations.
New Zealand law contains no such prohibition and the question of attribution to the acts or omissions of the related company is only one of four factors to be taken into account by the court in deciding on a contribution order.
Further under New Zealand law the court has express discretionary power to consider "any other matter it sees fit "when deciding whether it is "just and equitable to make the contribution order.

Given the extremely high bar attaching to section 599 it is little surprise that it is regarded as underutilised. Conceived as it was to wash out any " anti-business" provisions it is surely high time to level the playing field for both employees and unsecured creditors , who themselves may be companies . If there is a genuine concern that S 599 offers an avenue of redress then it must be one which is fair to all players and allows the court a real opportunity to consider what is fair and equitable in the circumstances prevailing. It was for that reason that ICTU proposed amending the section in 2017 and do so again.

ICTU Proposal

Delete section (5) and amend section 599 (4) as follows:

"in deciding whether it is just and equitable to make an order under this section the court shall have regard to the following matters:

(a) The extent to which the related company took part in the management of the company being wound up
(b) <u>The extent to which the circumstances that gave rise to the winding up of the company are attributable to the acts or omissions of the related company</u>
(c) The conduct of the related company towards the creditors and employees of the company being wound up
(d) The effect such order would be likely to have on the creditors of the related company concerned.
(e) <u>Any other matters it sees fit "</u>

Effect
The effect of this deletion and amendment would be to significantly level the playing field for all in liquidation as opposed to having the cards stacked in favour of certain sections of business to the detriment of not only employees but unsecured creditors, small business and the public interest. This is particularly so where assets have been removed in the circumstances posed by the question.

<u>S 608 Power of Court to order the return of assets improperly transferred</u>
Similarly with section 608 dealing specifically with the return of assets improperly transferred there is high onus of proof, not so much in the fact that there is" prima facie" reliance on "effect" rather than "intent". Rather it is that the effect of the disposal of an asset was to "perpetrate a fraud on the company, its creditors or members" (S608 (1) (b))
Essentially, as with s224 & 599, what the section gives with one hand it takes with the other, on this occasion, in the one sentence, given the extremely high bar with proving fraud.
Effectively what it means is that the court can only make an order returning the asset argued to be improperly removed if there is sufficient proof before it as to the perpetration of a fraud albeit by effect as opposed to intent.

The bottom line here is surely that the effect of the disposal was to deplete the assets of the company to the detriment of the creditors or members in circumstances where the person having use of, controlling or in possession of that asset or the proceeds of sale or development of same knew or ought reasonably to have known it would have such effect but proceeded nevertheless or was reckless as to that consideration.

ICTU proposal

Accordingly ICTU proposes amending S 608 (1) (b) by the deletion of the current sub section and its replacement as follows:

"The effect of such disposal was to deplete the assets of the company to the detriment of the company; its creditors or members in circumstances where the person disposing of the asset was reckless as its disposal or knew or ought to reasonably to have known it would have such effect but proceeded nevertheless to dispose of it."

Effect
The effect of this amendment would be render it more feasible to seek the return of assets improperly removed in the circumstances suggested by the question , to the benefit of employees and other creditors and the liquidation process itself.

4. Examine the legal provision that pertains to any sale to a connected party following insolvency of a company including who can object and allowable grounds of an objection.

S 604 Unfair preference: effect of winding up on antecedent and other transactions

We take this to be essentially a consideration around section 604 of the Act.

This section was previously considered by both Duffy/Cahill and the CLRG, and at S 6(4) makes particular reference to conveyances and other acts to connected persons within the 2 years previous to winding up.

Connected persons are defined by S559 (1) of the Companies Act as a person who at the time of the transaction to the company concerned was a director, shadow director, person connected with a director , a related company or a trustee of or surety or guarantor for the debt due to any of these persons.

In essence S604 appears to be a companion provision to S 608.
The section invalidates acts by conveyance, mortgage or delivery to any creditor or creditor trustee with a view to giving them preference over other creditors and shall be deemed unfair preference and invalid if the winding up of the company commences with 6 months of the act and the company being wound up is unable to pay its debts.

The particular sub section which deals with connected persons is SS (4) and it invalidates such acts in favour of a connected person if done within 2 years antecedent to the wind up.

ICTU Proposal

Amend the time limitations in S604 (2) & (4) to 12months and 4 years respectively.

Effect
The effect of these amendments would be to increase the reach of provision with regard to antecedent transactions and therefore be of dissuasive effect on persons contemplating such acts.

Insofar as the section covers transactions other than antecedent and the question posed concerns who can object to any such acts of conveyance etc., the ICTU view is as follows:

ICTU Proposal

Those who can object to any sale, antecedent or otherwise, to a connected party must include employee creditors and/or their representatives on their behalf.

The grounds of objection cover the general grounds of unfair preference, the effect on the viability of the company, the impact on employment and on the terms and conditions of employment as well as other considerations such environmental impact , civic impact and the impact on other more vulnerable SME trading entities.

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