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Bearers of bad news: what HR needs to know about insolvency

By Raoul Parekh and Ben Smith in Personnel Today - 30 September 2020

With so much economic strife and uncertainty on our doorstep, many HR leaders will have to take a deep breath and confront the difficult issues of company insolvency and administration. Raoul Parekh and Ben Smith, offer guidance.

These are difficult times for businesses in almost every sector, and sadly a rise in insolvencies and business failures has been widely predicted. When the worst happens, the human resources team will often play an important role. However, for many HR practitioners, this will be a new experience. This article provides a guide to the key things HR practitioners need to know, focusing on businesses entering into administration.

Signs of trouble ahead

The HR team will usually have good visibility that trouble is brewing. Management often puts in place cost-saving measures to reduce the risk of insolvency. This could involve the HR team being asked to help identify areas for restructuring and to establish the costs and cost savings of proposed redundancies. Other measures that could be put in place including reducing salaries and cutting working hours.

Rise like a phoenix

Administrators are appointed with three statutory objectives, one of which is to turn the company around so that it can be rescued as a going concern. Therefore, in an administration process it does not necessarily follow there will be large-scale job losses. It is common for administration to end in the sale of some or all of the business, with that sale sometimes negotiated and agreed in principle prior to the administration beginning. There are therefore several parallels between an administration process and other business transformations (for example, being acquired or merged). These transactions are good news, but present challenges even for seasoned HR professionals who are familiar with merger and acquisition transactions and business integrations, because:

- They happen fast. Insolvent purchases typically proceed at breakneck speed and with little time to prepare.
- Buyer beware. Insolvent businesses are “sold as seen”, with little advance information or contractual protection for the buyer.
- Corners have been cut. Inevitably, insolvent businesses will have had to reduce costs, sometimes through drastic action. Employment law breaches may have occurred and/or money may be owed to employees.
- The legal rules are different. When a business is bought out of administration very often TUPE will apply – but this is TUPE with a twist, and there are some changes to the usual rules to look out for.

In particular, the uncertainty and change can easily have a negative effect on employee morale, leading to the loss of key talent at the time when the business most needs stability. While some job losses are almost inevitable, HR and management should consider what retention measures can be put in place with employees, whether financial or softer.

Doing the groundwork

The speed of insolvency proceedings means that prior preparation is vital. We suggest taking the following steps if a sale of a business you support is on the horizon:

- Maintain an employee spreadsheet/HRIS. Keep up-to-date records of employees with job titles, salary, bonus/incentives, benefits, start date, notice period and date of birth. Ensure you round up contracts and up-to-date appraisal, sickness and disciplinary/grievance records, which will need to be handed over to the purchaser.
- Redundancy consultation. When insolvency looms, there is a tricky (but important) assessment to be made about whether and when to start redundancy consultations and notify potential redundancies to the government. Expert advice should be taken to avoid potential criminal liability.
- Gather information about redundancy payments. Even if redundancies are not imminent, a buyer will want to be clear about its obligations in a potential future redundancy situation. Gather up information about the approach taken historically, including details of any formula used to calculate payments, and any contractual commitments (for example, change of control provisions for senior staff).
- Analyse shared services. If part of the business is sold, the buyer will want to assess which employees will transfer under TUPE and will need information, particularly about “shared service” employees. Gather data on how much time individuals spend supporting different business units, how their cost is allocated and whether they are formally considered to be “point person” for a particular division.

Got to pay the bills …

Most employee debts are unsecured and rank second to last in the order of priority when the business’s assets are realised. However, if the contracts are adopted by the administrator, then certain employee liabilities will become “super priority” claims.

Certain employment debts are ranked higher, however, as employee creditors are owed their “remuneration” (capped at £538 per week) as a preferential debt. If the employer is unable to pay employment debts, the government – via the National Insurance Fund (NIF) – will pay out certain debts such as unpaid salary/benefits and unpaid holiday. This can be a crucial safety net for employees, but in most cases still only allows the recovery of a fraction of their full entitlement.

When an administrator is appointed, they will normally provide information to the employees about how to make a claim on the NIF and provide them with a reference number to use on the necessary forms. HR should expect to deal with various queries from employees on this topic, and so familiarising yourself with this process ahead of time is a good idea.

While insolvency is never an indication of financial health in a company, it is also often far from terminal. Leaders have a responsibility to try to preserve the core of a viable business if they can, and one way HR professionals can help that aim is by ensuring compliance with employment law to prevent unexpected liabilities. Morale is also vital during challenging trading conditions, and of course is very difficult to maintain when news is not good.

HR teams are often a channel to employee sentiment and the first port of call for those with welfare concerns. HR will be a vital part of any employer’s recovery and administration plans, and we hope this article will provide some of the tools to enable that.

Read the full article here.

