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ALERT

Boarding passes ready – when employees may unexpectedly move around within a corporate group

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The European Court of Justice (the "**ECJ**") has ruled that, in certain circumstances, when a subsidiary company is wound up, its employees will transfer automatically to its holding company.

What happened?

Air Atlantic SA ("**AIA**") was a Portuguese company operating in the aviation sector. It had been providing charter (or non-schedule) flight services since 1985.

On 19 February 1993, AIA was wound up. During the winding-up, several of AIA's employees were dismissed as part of a collective redundancy.

TAP – the Portuguese flag carrier – was the main shareholder in AIA. From 1 May 1993, TAP began operating some of the charter flights that AIA had agreed to provide up to 31 October 1993. In addition, TAP, which had not previously been active in the charter flights sector, began operating its own charter flights on the same routes used by AIA.

To do this, TAP used four aeroplanes that AIA had previously used on its charter flight routes. TAP also took on the burden of paying charges under the leasing contracts for those aeroplanes, and it appropriated certain office equipment that previously belonged to AIA.

Finally, TAP took back a number of employees it had previously seconded to AIA and assigned them to tasks that were virtually identical to the tasks they had carried out for AIA.

The claim

The employees launched a claim in the Lisbon Employment Court. They argued that AIA had effectively transferred its business to TAP. Under the EU Acquired Rights Directive, employees cannot be dismissed merely because of a transfer of a business. They alleged that the collective redundancy was connected with that transfer and so was unlawful.

The employees claimed that they should be re-instated in their employment in corresponding grades and be paid compensation. The Lisbon Employment Court found in their favour.

However, on appeal, both the Lisbon Court of Appeal and the Portuguese Supreme Court decided that there had been no transfer of a business and so the Acquired Rights Directive did not apply. According to the Supreme Court, the fact that a commercial activity is "merely continued" does not mean there has been a business transfer. The collective redundancy was therefore lawful and the Supreme Court struck the employees' claims out.

After further appeals, the Supreme Court asked the European Court of Justice to giving a ruling on whether there had in fact been a transfer of a business from AIA to TAP.

Why is this relevant to the UK?

Although the decision relates to a Portuguese claim, it ultimately revolves around the Acquired Rights Directive. The Acquired Rights Directive is a European Union Directive designed to protect rights that employees have accrued during their service to their employer. EU Member States are required to work the Directive into their national laws. In the UK, the Directive has been implemented in the form of "TUPE" (the Transfer of Undertakings (Protection of Employment) Regulations 2006).

TUPE most commonly applies where an organisation transfers a business or undertaking (or part of a business or undertaking) to another organisation (a "business transfer"). This usually happens on an acquisition or a disposal of a business, or when a business is shifted from one part of a corporate group to another.

(TUPE also applies where an organisation has outsourced services and the organisation decides to move those services from one provider to another, or to bring them back "in-house".)

When TUPE applies to a business transfer, the transferor's employees transfer automatically to the transferee along with the business. If either organisation dismisses the employees and the sole or principal reason for the dismissal is the transfer, the dismissal is automatically unfair unless the transferor can establish an economic, technical or organisational reason. This does not mean that an organisation cannot dismiss employees, but it will need to consider the potential costs of paying compensation for unfair dismissal.

In addition, on a business transfer, TUPE requires the transferor and the transferee to inform all affected employees and consult with recognised trade unions or elected representatives. This can add significantly to the time and costs of the transfer.

The ECJ's interpretation of the Acquired Rights Directive is therefore relevant to the UK, as it will influence how the courts interpret and apply TUPE on transfers of UK businesses.

What did the ECJ decide?

The ECJ decided that there had indeed been a business transfer. It gave several reasons:

- TAP took on AIA's charter flights, which indicated that TAP had taken over AIA's customers and there was virtually no suspension of activity.
- TAP developed its own charter flights on AIA's routes, which indicated that TAP was pursuing activities previously carried on by AIA.
- TAP took back seconded employees and assigned them identical tasks, which indicated that TAP took over some of AIA's staff.
- TAP used aircraft previously employed by AIA, which indicated that TAP had taken on assets essential for pursuing the activity previously carried on by AIA.

Strictly, the ECJ's decision is restricted to very specific circumstances: winding up an airline in the charter airline industry, where a shareholder takes on significant aspects of the charter airline's business. However, there is no reason to suspect the decision would be different in another sector.

What are the implications?

The ECJ's decision may have a bearing on how the English courts apply TUPE. TUPE does not apply if the company in question is in "terminal insolvency proceedings", so liquidators need not fret.

However, the decision has implications for groups of companies intending to wind solvent subsidiaries up. This could happen as part of a group reorganisation, where the group wishes to simplify its structure and/or consolidate different assets and businesses into single entities.

It could also happen as part of a restructuring, where a group's debt facilities are re-packaged into a new financing entity. It may be that assets or businesses are transferred as part of that restructuring, and this may be enough to amount to a transfer of a business.

In each case, it is important to look carefully at which assets and contracts are likely to end up with which entities. TUPE could apply even if there is no formal sale arrangement and the transfers simply take the form of distributions of assets, or, even more informally, if one group entity simply starts "using" the wound-up company's assets and adopting its contracts. This may well be enough to activate TUPE and transfer the employees over to another group entity.

The result could be a messy mish-mash of employee and pension arrangements, with employees being employed by the "wrong" companies. Worse still, companies that dismiss employees as part of a reorganisation or restructuring may find the employees have a claim for automatic unfair dismissal.

Finally, companies would need to initiate a formal inform-and-consult process, involving (in some cases) discussions with a trade union or the election of employee representatives. This can be time-consuming, with the potential to delay a fast reorganisation or restructuring.