

LEGAL UPDATE

Attorney General of the CJEU: Employees protected when applying a pre-pack

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Pre-packs have been keeping the Dutch legislature and case law quite busy in recent years. For some time, the question has been whether, in the case of an insolvency restart prepared by means of a pre-pack, the insolvent entity's staff automatically transfer to the restarting entity. Normally, in an insolvency, the employment law regulations on the transfer of an undertaking do not apply and therefore the staff does not automatically transfer to the restarting entity. The fact is that the Netherlands opted not to apply the rules on the transfer of an undertaking in insolvency (Article 5 of Council Directive 2001/23/EC). However, is this also the case if the restart has already been meticulously prepared before the insolvency?

Supreme Court refers questions for preliminary rulings

Last year, the Supreme Court referred questions for preliminary rulings to the Court of Justice of the European Union in connection with the insolvency of shrimp processor Heiploeg (2014), which had been pronounced after a pre-pack. These questions related to the employment law protection of employees when applying the pre-pack. In short, the Supreme Court's question was whether the protection under employment law that exists in the event of a transfer of an undertaking also applies in the event of an insolvency restart where this restart has already been prepared by means of a pre-pack before the declaration of insolvency.

On 9 December 2021, the Attorney General ("AG") advised the Court of Justice on answering this question. The answer is summarised as follows:

'Article 5 of the Directive must be interpreted as meaning that a pre-pack - in which the transfer of the undertaking, prior to the declaration of insolvency, is prepared down to the smallest detail to enable a rapid restart after the declaration of insolvency, thus avoiding the interruption of activities, in order to preserve the value of the company and employment - does not meet the conditions required for an exception to the safeguarding of rights granted to employees in Articles 3 and 4 of this Directive.'

Thus, the AG is of the opinion, that when applying the pre-pack (unlike a regular insolvency without preparation) there is no justification for limiting the employment law protection of the insolvent entity's employees. The protection afforded by the Directive should remain in place when a pre-pack is applied. This means that there is then a transfer of undertaking and that the insolvent entity's employees transfer to the acquiring entity by operation of law. The AG considers it irrelevant that a pre-pack aims, in principle, at obtaining the highest possible proceeds for the joint creditors of the company, or that the insolvency of the transferor (even without application of the pre-pack) is inevitable.

The Court of Justice's decision in the *Smallsteps* case

The questions referred for preliminary rulings in the *Heiploeg* case follow on from an earlier set of proceedings before the Court of Justice, which also focused on a pre-pack construct. In that case (*Smallsteps*), the Court of Justice also ruled - though with significantly less nuance - that a restart after a pre-pack constituted a transfer of an undertaking. Employees' rights under the Directive were therefore safeguarded. However, the Court (implicitly) based this finding on the fact that a restart *in itself* (whether prepared or not) was not made with a view to liquidation and therefore did not meet the exception conditions of Article 5 of the Directive in the first place. In other words: the Court's decision

unintentionally had a broader scope than just a restart after a pre-pack. That would mean that in any restart, all employees of the insolvent entity would transfer to the acquiring entity.

The AG's statements in the *Heiploeg* case seem more nuanced and the answer was more focused on the pre-pack, rather than the practice of restarting in general. But this still does not lead to a different conclusion than in the *Smallsteps* case. Because a restart in a pre-pack is meticulously prepared in advance, the subsequent insolvency proceedings are no longer aimed at liquidating the company's assets. This is a condition for excluding a transfer of undertaking (Article 5 of the Directive). Since that condition is not met, the employment law protection of the Directive must remain effective when the pre-pack is applied.

Conclusion

The AG's position is now known. All we can do now is await the Court's decision. Meanwhile, the Dutch legislature is preparing the Act on the Transfer of Undertakings in Insolvency (*Wet overgang van onderneming in faillissement*). The bill was already subjected to consultation in 2019. It is not yet known when the bill will be presented to the Lower House. If the bill is adopted, new rules on the transfer of employees will also apply to "ordinary" restarts. Thus, it is possible that significant changes in the area of employees' rights in insolvency will follow in the coming years. We are following developments closely and will keep you informed.

This is a Legal Update by Rhea Bask.

For more information, please contact:

Rhea Bask
+31 30 25 95 567
rheabask@vbk.nl