Neutral Citation Number: [2020] EWCA Civ 600

Case No: A2/2020/0631

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
Mr Justice Trower
CR-2020-002113

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 6 May 2020

Before:

THE CHANCELLOR OF THE HIGH COURT
LORD JUSTICE BEAN
and
LORD JUSTICE DAVID RICHARDS

- -

IN THE MATTER OF DEBENHAMS RETAIL LIMITED
(IN ADMINISTRATION)

and
IN THE MATTER OF THE INSOLVENCY ACT 1986

(1) GEOFF ROWLEY
(2) ALASTAIR MASSEY
(as Joint Administrators of Debenhams Retail Limited)
Appellants

- -
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Tom Smith QC and Richard Fisher QC (instructed by **Freshfields Bruckhaus Deringer LLP**) for **the Appellants**

Hearing date: 22 April 2020

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Approved Judgment

Lord Justice David Richards (giving the judgment of the Court):

Introduction

1. Following the hearing of this appeal, we announced on 24 April 2020 that the appeal was dismissed, for reasons to be given later. In this judgment, we give our reasons.

2. The appeal concerns the inter-relationship between the Government's Coronavirus Job Retention Scheme (the Scheme) and the "adoption" of contracts of employment by administrators under the Insolvency Act 1986 (the Act). Specifically, the issue is whether by paying only the amounts which may be claimed under the Scheme to employees while they are "furloughed" under the Scheme and therefore not permitted to work for the Company, the administrators have adopted the contracts of those employees.

3. In summary, the effect of the adoption of a contract of employment is that the wages or salaries, together with some other amounts such as sick pay and holiday pay, for the period after adoption until termination of the employment or, if earlier, the end of the administration, are payable as expenses of the administration ahead of not only pre-administration unsecured liabilities but also many of the costs and expenses of the administration.

4. We refer in more detail to the Scheme below, but its essential feature is that the Government will reimburse or fund a proportion of the salaries of employees who are furloughed as a result of the measures taken to combat the Covid-19 pandemic.

The facts

5. Debenhams Retail Limited (the Company) is part of a group which carries on retail business, principally through department stores. The Company has some 15,550 employees. Following the introduction of lockdown measures by the Government to combat the spread of the Covid-19 infection, the Company closed its stores and on 25 March 2020 wrote to approximately 13,000 employees, informing them that they were being placed on furlough under the Scheme. A further 867 employees were similarly furloughed in the following days.

6. On 9 April 2020, administrators of the Company were appointed under schedule B1 of the Act by the directors of the Company. This provides protection to the Company by means of a moratorium against actions against the Company and its property by creditors. The purpose of the administration is to seek to rescue the Company as a going concern. The administrators have consented to management continuing to exercise their functions, with the aim of resuming trading from its stores once the lockdown measures are lifted.

7. The administrators considered that the purpose of the administration would be best furthered if the employees remained on furlough under the Scheme. They would continue to pay salaries up to the limits reimbursed or funded under the Scheme, but they would not make any further payments to top up salaries. They wrote on 10 April 2020 to all or most of the furloughed employees seeking their express consent to being furloughed and to the consequent reduction in pay. By the hearing of the appeal,

express consents had been received from 13,056 employees, with 10 employees having failed to reply and 4 employees refusing to give their consent.

The proceedings

8. By an application notice issued on 10 April 2020, the administrators sought directions under paragraph 63 of schedule B1 to the Act as to whether by participating in the Scheme they would be adopting the contracts of the furloughed employees. They sought a declaration as follows:

> "None of the contracts of employees who have been furloughed will be adopted by the Joint Administrators if the employees remain furloughed and the Joint Administrators take no further action in relation to these employees except for issuing such communications as may be required to confirm the terms of the employees' ongoing engagement and to seek any required consent in relation to such terms and to pay to the furloughed employees amounts that are to be reimbursed to the Company through its participation in the Coronavirus Job Retention Scheme."

9. The application was heard by Trower J on 15 April 2020. On the same day, he announced his decision, declining to make the declaration sought by the administrators and holding that it was likely that they would be found, in the circumstances contemplated by the declaration, to have adopted the contracts of employment of the furloughed employees. He declared and directed that the administrators be at liberty to act on that basis. He handed down a reasoned judgment two days later, on 17 April 2020.

10. The order made by the judge was in the following terms:

> "The Joint Administrators be at liberty to act on the basis that they will be taken to have adopted (for the purpose of and within the meaning of paragraph 99(5) of schedule B1 to the Act), any contract of employment between the Company and its employees in circumstances where, in respect of any particular employee or employees, at any time after 14 days after the time of their appointment:
>
> (1) the Joint Administrators cause the Company to make payments to such employee or employees under and in accordance with their employment contracts including in respect of amounts which may reimbursed to the Company by a grant under the Scheme; or
>
> (2) the Joint Administrators make an application in respect of such employee or employees under the Scheme."

11. The submissions on behalf of the administrators on this appeal have focussed on the consequences of the making of payments by the administrators, as envisaged in paragraph (1) of the order. No separate submissions were addressed to paragraph (2).

12. In the absence of any respondent to the administrators' application, in particular any employee of the Company, the judge for good reason did not feel it was right to make a declaration in final terms as to whether the contracts of employment would be adopted. The order he made was nonetheless of value because it provided a practical answer to the question and it permitted the administrators to proceed on the stated basis, without risking any personal liability to creditors or others for doing so.

13. In doing this, the judge followed the course adopted by Snowden J on 9 April 2020 when he gave similar directions on an application by the administrators of Carluccio's Limited, which has a chain of over 70 restaurants with some 2,000 employees. The restaurants had closed in accordance with the lockdown measures and an administration order was made by the court on 30 March 2020. As recorded by Snowden J in his judgment at [13], the administrators' strategy was to "mothball" the business and to seek a sale of it. As part of that strategy, they wished to put the employees on furlough under the Scheme. Snowden J heard the application in parts over 6-9 April 2020. Again, there was insufficient time to serve employees or to join a representative employee, but the judge heard submissions made by leading and junior counsel instructed by Unite the Union. Snowden J handed down a reasoned judgment on 13 April 2020: see *Re Carluccio's Limited* [2020] EWHC 886 (Ch) (*Carluccio's*).

14. As was the position before Trower J, we heard no opposing submissions, but we had the advantage of the judgments at first instance in this case and in *Carluccio's.* rejecting in each case the administrators' submissions. We were told that the Government had been informed of the application before Trower J and of the present appeal.

15. We would like to pay tribute to the comprehensive and careful judgments given by Snowden J and Trower J, which have been of great assistance to us and are all the more impressive for the speed with which they were produced in difficult circumstances.

The Scheme

16. The Scheme was announced by the Chancellor of the Exchequer on 20 March 2020. The statutory basis for the Scheme is a direction given by HM Treasury to the Commissioners for HM Revenue and Customs (HMRC) on 15 April 2020, pursuant to sections 71 and 76 of the Coronavirus Act 2020 (the Direction). HMRC have issued guidance statements, initially on 26 March 2020 and subsequently updated on a number of occasions. The directions and the more recent iterations of the guidance post-date both judgments, but they do not contain any changes material to the issue on the appeal.

17. Paragraph 2 of the Direction, headed "Purpose of scheme", includes the following:

> "2.1 The purpose of CJRS is to provide for payments to be made to employers on a claim made in respect of them incurring costs of employment in respect of furloughed employees arising from the health, social and economic emergency in the United Kingdom resulting from coronavirus and coronavirus disease.

> 2.2 Integral to the purpose of CJRS is that the amounts paid to an employer pursuant to a claim under CJRS are only made by way of reimbursement of the expenditure described in paragraph 8.1 incurred or to be incurred by the employer in respect of the employee to which the claim relates."

18. The Guidance issued by HMRC states that the Scheme "is designed to help employers whose operations have been severely affected by coronavirus (COVID-19) to retain their employees and protect the UK economy. However, all employers are eligible to claim under the scheme and the government recognises different businesses will face different impacts from coronavirus."

19. The expenditure subject to reimbursement is (i) the gross amount of earnings, subject to a maximum of 80 per cent or £2,500 per month (whichever is less), (ii) employer National Insurance contributions in respect of those earnings, and (iii) minimum automatic enrolment employer pension contributions. Employers may top up salaries beyond these limits, but they are not obliged by the terms of the Scheme to do so.

20. The following further features of the Scheme are important for this appeal.

21. First, the furloughed employees remain employed by their employer.

22. Second, a furloughed employee must be instructed to cease all work for the employer for 21 days or more. While the Direction issued by the Treasury states that the cessation of work must be agreed in writing by the employee (para. 6.7), the guidance notes issued by HMRC state only that the employee must be informed in writing, but nothing turns on this for the purposes of the appeal.

23. Third, furloughed employees may do other paid or voluntary work, but only if permissible under their contracts of employment. As they remain employees, they remain bound by their contracts of employment, save as regards working and attending for work.

24. Fourth, the payments made to employees, as reimbursed or funded by the Government under the Scheme, are salaries or wages. They are subject to income tax in the hands of the employees. They are expenses of the employer's trade for corporation tax purposes and the commensurate funds received from the Government are income for those purposes.

25. Fifth, if the employer seeks funds under the scheme in order to pay employees, the funds received must be used for that purpose.

26. Sixth, the guidance anticipates what will happen when the Scheme ceases, stating: "When the government ends the scheme, you must make a decision, depending on your circumstances, as to whether employees can return to their duties. If not, it may be necessary to consider termination of employment (redundancy)".

27. Seventh, the guidance provides expressly that an administrator of a company is able to access the Scheme and states that "we would expect an administrator would only access the scheme if there is a reasonable likelihood of rehiring the workers. For instance, this could be as a result of an administration and pursuit of a sale of the

business.". The guidance is not written in legal terms and Mr Smith QC, appearing for the administrators, accepted that the reference to "rehiring" was not to be taken to mean that the employees' contracts of employment had been terminated. That would be contrary to the whole thrust of the Scheme and it is not suggested that there is a separate regime for companies in administration.

The effect of adoption of a contract of employment

28. The effect of the "adoption" of a contract of employment by administrators is contained in paragraph 99 of schedule B1 to the Act which provides:

> "*Vacation of office: charges and liabilities*
>
> 99 (1) This paragraph applies where a person ceases to be the administrator of a company (whether because he vacates office by reason of resignation, death or otherwise, because he is removed from office or because his appointment ceases to have effect).
>
> (2) In this paragraph—
>
> "the former administrator" means the person referred to in sub-paragraph (1), and
>
> "cessation" means the time when he ceases to be the company's administrator.
>
> (3) The former administrator's remuneration and expenses shall be—
>
> (a) charged on and payable out of property of which he had custody or control immediately before cessation, and
>
> (b) payable in priority to any security to which paragraph 70 applies.
>
> (4) A sum payable in respect of a debt or liability arising out of a contract entered into by the former administrator or a predecessor before cessation shall be—
>
> (a) charged on and payable out of property of which the former administrator had custody or control immediately before cessation, and
>
> (b) payable in priority to any charge arising under sub-paragraph (3).
>
> (5) Sub-paragraph (4) shall apply to a liability arising under a contract of employment which was adopted by the former administrator or a predecessor before cessation; and for that purpose—

> (a) action taken within the period of 14 days after an administrator's appointment shall not be taken to amount or contribute to the adoption of a contract,
>
> (b) no account shall be taken of a liability which arises, or in so far as it arises, by reference to anything which is done or which occurs before the adoption of the contract of employment, and
>
> (c) no account shall be taken of a liability to make a payment other than wages or salary.
>
> (6) In sub-paragraph (5)(c) "wages or salary" includes—
>
> (a) a sum payable in respect of a period of holiday (for which purpose the sum shall be treated as relating to the period by reference to which the entitlement to holiday accrued),
>
> (b) a sum payable in respect of a period of absence through illness or other good cause,
>
> (c) a sum payable in lieu of holiday,
>
> (d) . . . . . , and
>
> (e) a contribution to an occupational pension scheme."

29. Paragraph 99(5) replaced section 19(5) of the Act, which itself, together with section 44 dealing with the position of administrative receivers appointed by debenture holders, had been introduced to reverse the effect of the decision in *Nicoll v Cutts* [1985] BCLC 322. It was held in that case that an employee who continued to work under an existing contract of employment after the appointment of a receiver had no claim to priority for the payment of his salary for the period after the receiver's appointment.

30. The effect of the relevant provisions of paragraph 99 was helpfully summarised by Mr Smith as involving the following points:

    (1) A liability arising under a contract of employment which is adopted by an administrator is charged on and payable out of the property of which the administrator has custody or control immediately before the cessation of his appointment (paragraph 99(3)).

    (2) The liability ranks ahead of the administrator's remuneration and expenses and any amounts secured by a floating charge, which themselves rank ahead of ordinary unsecured liabilities, and is therefore commonly described as enjoying "super-priority" (paragraph 99(4)).

    (3) The liability is restricted to "wages or salary" and excludes any liability which arises by reference to anything which is done, or which occurs, before the adoption of the contract (paragraph 99(5)). Wages or salary includes holiday

pay and sick pay (paragraph 99(6)), but has been held not to include redundancy payments and payments for unfair dismissal (*Re Allders Department Stores Ltd* [2005] EWHC 172 (Ch), [2005] ICR 867, [2006] 2 BCLC 1) or protective awards or payments in lieu of notice (*Re Huddersfield Fine Worsteds Ltd* [2005] EWCA Civ 1072, [2005] 4 All ER 886).

(4) The administrator is given an initial 14-day period following appointment to decide on the action, if any, to be taken. Any action taken within that period does not amount or contribute to the adoption of a contract (paragraph 99(5)(a)).

31. Because of the terms agreed with the vast majority of employees of the Company, wages or salary in excess of the amounts payable under the Scheme will not enjoy super-priority. Despite those terms, it is or may be the case that entitlements to full holiday pay will enjoy super-priority. Over a three-month period, the excess holiday pay not covered under the Scheme would amount to some £1.28 million.

Meaning of "adoption"

32. The Act contains no definition of the "adoption" of a contract of employment by an administrator or receiver. It was an issue considered by the House of Lords in *Powdrill v Watson, Re Paramount Airways Ltd* [1995] 2 AC 394 (*Paramount*).

33. In *Paramount*, the House heard three appeals, raising much the same issues. The appeal in *Paramount* itself was from a decision of the Court of Appeal (reported at [1994] ICR 395 and [1994] BCC 172) concerning a company in administration. The other two appeals were leapfrog appeals from a decision of Lightman J (reported with the House of Lords' decision) concerning two companies, Leyland DAF Limited and Ferranti International plc, which were in administrative receivership. For present purposes, the statutory provisions governing these two different processes are the same, save that administrative receivers but not administrators become personally liable on contracts of employment adopted by them, for which they have a statutory indemnity out of the assets of the company (section 44 of the Act).

34. There was one crucial difference between the facts in each of those appeals and the facts in the present case. In those cases, the relevant employees had all performed services for their employers after the expiry of 14 days from the appointments of the administrators or receivers, for which they had been paid. On those facts, it would be difficult, if not impossible, to contend that their contracts of employment had not been adopted, were it not for the letters that the officeholders had written to the employees in terms that were then standard. In those letters, the officeholders stated that they were not adopting the contracts of employment and were not assuming any personal liability for any sums that might fall due under them. The issue for the House as regards adoption was whether these letters had the effect that the contracts of employment had not been adopted. A further, and important, issue concerned the sums due under the contracts which enjoyed super-priority or for which the receivers would be personally liable, an issue that does not arise on the present appeal.

35. There are two submissions of counsel which are important to note before coming to the speech of Lord Browne-Wilkinson, with which the other members of the House agreed.

36. First, as reported at pp. 418-419, Mr Sumption QC for the appellant administrators and receivers submitted that adoption must refer to something that the office-holder causes the company to do and that "[a]s a matter of ordinary language, and in the particular legal context in which it appears in sections 19 and 44, adoption signifies some words or conduct on the part of the officeholder that objectively construed, evince an election to treat the relevant debt or liability as an expense of the administration or receivership rather than as an unsecured claim against the company". That was the springboard for Mr Sumption's submission that in the cases under appeal the officeholders had by their letters, objectively construed, evinced an election not to treat liabilities under the employment contracts as expenses, rather than as unsecured claims.

37. Second, as reported at pp. 427 and 428, counsel for the employees of Leyland DAF and Ferranti submitted that, by simply allowing contracts of employment to continue and by not giving notice of termination, officeholders adopt the contracts.

38. Much of Lord Browne-Wilkinson's speech concerns the precise liabilities under an employment contract which achieve super-priority if it is adopted. But, because of the reliance on the letters written by the officeholders to employees, he was also concerned with the meaning of the "adoption" of an employment contract in this context.

39. Lord Browne-Wilkinson first dispelled the notion that, by doing nothing, an officeholder adopted an employment contract. It was not necessary, to avoid adoption, for the officeholder to give notice of termination before expiry of the 14 days after appointment or at all. As he said at p.448G, "the mere continuation of the employment *by the company* does not lead inexorably to the conclusion that the contract has been adopted *by the administrator or receiver*" (emphasis added). The company is the employer. The question is not whether the employment continues, but whether the officeholder has adopted the employment contract.

40. In a passage at p.449A-B that forms the cornerstone of the administrators' submissions in the present appeal, Lord Browne-Wilkinson said:

> "In my judgment as Mr Sumption submitted adoption in sections 19 and 44 can only connote some conduct by the administrator or receiver which amounts to an election to treat the continued contract of employment with the company as giving rise to a separate liability in the administration or receivership."

41. By "a separate liability in the administration", Lord Browne-Wilkinson was referring to those liabilities under a contract of employment that enjoyed super-priority. All liabilities arising under an employment contract would be liabilities of the company but only some of them would be separate liabilities in the administration, enjoying super-priority, and only then if the administrator had adopted the contract.

42. Lord Browne-Wilkinson then considered whether it was open to the officeholder to limit, as the administrators and receivers had sought to do in their letters to the employees, the extent to which they adopted the contracts, concluding that they could not do so. The acceptance of Mr Sumption's submission excluded the words, vital to

the appellants' case, that adoption "signifies some *words or* conduct". If the officeholders' *conduct* constituted adoption, there was nothing they could unilaterally *say* to qualify or exclude adoption. (That is not to say that if officeholders informed employees that their contracts were being adopted, they would not be bound by that.)

43. In setting out his reasons for his conclusion, Lord Browne-Wilkinson said at p.449G-H:

> "Therefore the concept of adoption of the contract is inconsistent with an ability to pick and choose between different liabilities under the contract. The contract as a whole is either adopted or not: the consequences of adoption are then spelt out by the Act. If the employment is continued for more than 14 days after the appointment of the administrator or receiver, there seems to be no escape from the conclusion that the whole contract has been adopted."

He continued at p.450B-C:

> "…the contract of employment is inevitably adopted if the administrator or receiver causes the company to continue the employment for more than 14 days after his appointment."

44. Having at pp.450-452 analysed the particular liabilities under the contracts which achieved super-priority as a result of adoption, Lord Browne-Wilkinson summarised the position at p.452C:

> "I therefore reach the following conclusions: (a) for the purposes of both section 19 and section 44 an employee's contract of employment is "adopted" if he is continued in employment for more than 14 days after the appointment of the administrator or receiver; (b) it is not possible for an administrator or receiver to avoid this result or alter its consequences unilaterally by informing the employees that he is not adopting their contracts or only doing so on terms; (c) in the case of both administration and receivership the consequence of adoption of contracts of employment is to give priority only to liabilities incurred by the administrator or receiver during his tenure of office."

45. The phrases "the employment is continued" and "he is continued in employment" at pp.449 and 452 respectively refer to the conduct of the officeholder in continuing the employment, as Lord Browne-Wilkinson himself said in the passage from p.450B-C quoted above.

46. For the administrators in the present case, Mr Smith submitted that the passage at p.449A-B quoted above, where Lord Browne-Wilkinson endorses Mr Sumption's submission, represented the *ratio* of the decision in *Paramount*. It followed that, before it could be concluded that contracts of employment had been adopted, there must be demonstrated (i) words or conduct on the part of the administrators (we have earlier commented that Lord Browne-Wilkinson refers only to conduct); (ii) which,

objectively construed, evidences an election on the part of the administrator; (iii) to treat the liabilities arising under the contract of employment as enjoying super-priority. Mr Smith correctly accepted that such election was to be judged objectively, and not by reference to the subjective intentions of the administrators.

47. Mr Smith submitted that, if an administrator actually pays wages, it is normally reasonable to infer that *he wishes* the employee to continue working and that he will pay the wages that fall due. Likewise, if the administrator expressly or impliedly requests the provision of services, it is usually a reasonable inference that *he is agreeing* to pay those wages in full as an expense of the administration. Although Mr Smith accepted that the test is to be applied objectively, his submissions involve a test of what the administrator can be taken to have wished or agreed. In other words, it is an objective assessment of the administrator's state of mind, judged by his words and conduct.

48. Mr Smith discerned a difference in approach to the test for adoption between Trower J in the present case and Snowden J in *Carluccio's*.

49. Snowden J said in *Carluccio's* at [84] that Lord Browne-Wilkinson's summary at p.452C was "shorthand for the same concept that he had described" at p.449A-B. At [91], Snowden J held that as and when the administrators made an application under the Scheme or made payments to the employees who had consented to be furloughed, they "would be doing an act which could only be explicable on the basis that they were electing to treat the varied contract as giving rise to liabilities which qualify for super-priority".

50. While Mr Smith submitted that Snowden J had correctly analysed the test established by *Paramount*, he argued that Snowden J had misapplied it. Either making application under the Scheme or paying remuneration to furloughed employees were entirely explicable without any election to treat liabilities as having super-priority, because the remuneration would be reimbursed or funded by the Government and the payments thus had no impact on the administration estate. The administrators therefore did "not need to make any election" to treat the liabilities as having super-priority. This is consistent with Mr Smith's approach of arriving at an objective assessment of the intentions of the administrators.

51. Mr Smith submitted that in the present case Trower J applied the wrong test. At [52] the judge said that "Lord Browne-Wilkinson contemplated that, by continuing to cause the company to treat a person as an employee by any action taken subsequent to the expiry of the 14 days period, the contract of employment will have been adopted". What was needed was conduct on the part of the administrator which could be said to amount to an election to treat the contracts as continuing: see [53]. At [64], the judge said that in his view it was plain that by participating in the Scheme and paying remuneration to furloughed employees the Company "comes under a separate liability incurred in the administration which flows from the continued existence of the contract. It arises in circumstances in which the Administrators elected to take steps which require them to treat the contract as continuing to give rise to liabilities to which the Company is subject in its administration."

52. We do not accept that these judgments display any significant difference in approach. They were expressed in different terms, as is to be expected, particularly because, as

Trower J observed at [44], it is not clear that the submissions made on behalf of the administrators in the two cases were the same.

53. In our judgment, Mr Smith's submissions misunderstand the approach taken by Lord Browne-Wilkinson in *Paramount*. When Lord Browne-Wilkinson referred at p.449A-B to "some conduct by the administrator or receiver which amounts to an election to treat the continued contract of employment as giving rise" to super-priority, he was not introducing as a relevant factor the intentions of the administrator, even if objectively determined. He did not, as Mr Smith submitted, require the conduct of the administrator to *evidence* an election by the administrator. It is a question of law: is the conduct of the administrator such that he must be taken to have to accept that the relevant amounts falling due under the employment contract enjoy super-priority? It is a wholly objective question, focussed entirely on the conduct of the administrator. As Lord Browne-Wilkinson repeatedly said, the issue is whether the officeholder has "continued" the employment of the relevant employees. This is the essence of the test propounded by him. If the officeholder has continued their employment, in other words has taken active steps to continue their employment, that necessarily results in super-priority for the relevant liabilities under the contracts of employment. As earlier noted, and by contrast, doing nothing involves no continuation *by the administrators* of the employment.

54. We agree with the way in which Laddie J summarised the effect of *Paramount* on the meaning of adoption in *Re Antal International Ltd* [2003] EWHC 1339 (Ch), [2003] 2 BCLC 406 at [7]:

> "What Lord Browne-Wilkinson was pointing out was that it was important to find some conduct on behalf of the administrator or receiver which could be treated as an election or could be regarded as him exercising a choice as to whether or not the contracts of employment were to be adopted."

And again at [12] where he said:

> "It is necessary to look at the facts and to decide whether there has been some conduct by the administrator or receiver which can legitimately be treated as an election to continue the contract of employment."

Adoption of employment contracts in the present case

55. The issue is therefore whether the administrators have continued the employment of the furloughed employees. That is an issue to be decided by reference to the evidence before the court in the particular case.

56. The following facts tend to support the conclusion that the administrators have continued the employment of the furloughed employees.

57. First, the administrators will continue to pay the wages or salaries of the furloughed employees up to the limits provided by the Scheme. Those will be payments of remuneration pursuant to their contracts of employment, subject only to the limits. The employees' entitlement to those payments is derived exclusively from their

contracts. This is reflected in the tax position of both the employees and the Company. The remuneration will be income in the hands of the employees, chargeable to income tax (which will, in all or most cases, be collected through the PAYE system). The remuneration will be an expense of the Company's trade and the payments by the Government under the Scheme will be income of the Company, for corporation tax purposes.

58. Second, all the furloughed employees who have accepted the continuation of their employment on these terms (and those other employees who do not treat their contracts as terminated by reason of the Company's failure to pay their full contractual remuneration) will remain bound by their contracts of employment, save only as regards the obligation to be available for work during the furlough period. For example, as the Scheme states, furloughed employees are free to undertake voluntary or paid work for others, but only if permissible under their employment contracts. They remain bound by duties of loyalty and the like. They will remain available, and they will be obliged, to provide their services to the Company as and when it is able to re-open its stores.

59. Third, in continuing to pay the furloughed employees, the administrators are acting with the objective of rescuing the Company as a going concern, that being the purpose of the administration, and in the interests of the Company's creditors as a whole: see paragraph 3(1) and (2) of schedule B1. The administrators rely on paragraph 66 of schedule B1 to continue to pay the remuneration of the furloughed employees but to do so they must think "it likely to assist achievement of the purpose of administration".

60. Mr Smith relied on three principal points for the opposite conclusion. First, the employees are not and will not be providing any services to the Company. It is a condition of the Scheme that they do not do so. Second, while they are furloughed, the employees' remuneration is limited to that which is covered by the Scheme. The effect is therefore neutral as regards the administration estate. All payments made to the furloughed employees will be reimbursed to the Company under the Scheme or, once there are insufficient funds in the Company, the payments will be made out of the funds provided by the Government under the Scheme. As a matter of economic substance, the Company is the conduit for Government funds. Third, any decision whether to terminate the contracts of furloughed employees will be made only once the Scheme has ended. What that decision will be, as regards any employees, is presently impossible to predict and will depend on the circumstances when the Scheme ends. This is consistent with the basic aim of the Scheme, to prevent redundancies as a direct result of the lockdown.

61. As to the first factor, the furloughed employees are not carrying out any work for the Company, and indeed are not permitted to do so under the terms of the Scheme. This is clearly a significant factor, and one that distinguishes the present case from *Paramount*. It is not, however, one that is sufficient by itself. In his judgment in *Carluccio's*, Snowden J gave this example at [72]:

> "…take an employee who has particular skills or know-how regarding the company's business which would, if available to a competitor, devalue the business which the administrator was seeking to sell. Even if there was no new work for the

> employee to do in the administration until it was known whether the business could be sold, it would be commercially important for the administrator not to terminate the employee's contract. In that way, the employee would continue to be available to the purchaser of the business, the restrictive covenants in his contract would continue in effect, and the maximum post-termination period of restraint would be available for the potential benefit of the purchaser. Given those benefits to the administration, even if, with the permission of the administrator, the employee were not required to attend the premises to work, it would be wrong if they were not entitled to payment of their wages or salary [as a super-priority expense]."

62. Mr Smith accepted, correctly in our view, that Snowden J was right in that example to conclude that the administrator would have adopted the contract of employment. While the enforced non-provision of services under the Scheme is a relevant factor, it is not decisive and must be balanced against the continued performance of the employment contracts by both sides in all other respects, save for the limit on remuneration, and against the administrator's purpose in continuing with the employment contracts and the potential benefit to the administration.

63. The second factor on which Mr Smith relied was that, while the employees are furloughed, their remuneration is limited to the amounts payable under the Scheme. The effect is therefore neutral as far as the administration is concerned. In economic terms, the Company is a conduit for the payment of Government funds to the employees. We do not consider that this is a well-founded point. The legal analysis is clear, as explained above. The furloughed employees remained employed and they are paid the remuneration due under their contracts, subject to the maximum under the Scheme. The remuneration is an expense of the Company and the Government grants are income of the Company. The Government could have devised a furlough scheme which did not involve using the employer as the conduit for the remuneration, but it did not do so. The legal consequences of the Scheme must be decided by reference to its actual terms.

64. The third factor is that any decision to terminate the furloughed employees' contracts is postponed until after the Scheme has ended. What that decision will be, as regards any employees, is presently impossible to predict and will depend on the circumstances when the Scheme ends. The short answer to this is that in the meantime the administrators have themselves taken steps to keep the contracts in being. They have done so in the hope, for which there must exist reasonable grounds, that the employees will be able to resume work under their contracts either during the administration or on its successful conclusion.

65. We are satisfied, having considered these competing factors, that the administrators have clearly adopted the contracts of the furloughed employees.

66. We have earlier referred to the administrators' stated reliance on paragraph 66 of schedule B1 as the statutory authority for paying the wages or salaries of furloughed employees.

67. The question of the authority for paying wages or salaries was raised in *Carluccio's*. Snowden J took the view that paragraph 99 was the provision "specifically designed to deal with the ability and obligation of administrators to pay wages or salaries to employees in an administration". Without completely ruling out paragraph 66 as a source of authority, he considered that analysis of the authority to pay remuneration must begin with paragraph 99: see [55]-[56] and [111]-[112]. He accordingly considered that it would promote the rescue culture which underlies schedule B1 if paragraph 99 were interpreted to include the contracts of furloughed employees; see [73]-[74].

68. We agree with Mr Smith's submission that paragraph 66 is an appropriate and perhaps the most obvious source of authority for these payments. The condition for payments under that paragraph, that the administrators think that the steps they are taking will be "likely to assist achievement of the purpose of administration", will necessarily be satisfied. In contrast, by its terms, paragraph 99 operates only where a person ceases to be the administrator, although it may well the case, as Trower J observed at [40]-[41], that authority can also be derived from paragraph 99.

69. While we agree with Snowden J's conclusion that on the proper construction of paragraph 99 the administrators had adopted those contracts, we do not accept it is supported by reliance on paragraph 99 as the authority for the payment of remuneration. However, as he himself made clear, it was not an essential part of his decision.

Conclusion

70. Overall, for the reasons we have given, which do not essentially differ from those given by Trower J at [51]-[65], we conclude that the administrators have, for the purposes of paragraph 99, adopted the contracts of those employees who have consented to be furloughed. For these reasons, we dismissed the appeal.

71. Mr Smith very fairly outlined to us the difficulties that may face administrators in deciding whether to take the steps necessary to retain furloughed employees, or to place employees on furlough, if (as we have held) that will involve adoption of their employment contracts. In the present case, and it appears also in *Carluccio's*, the administrators have been able to agree terms with the vast majority of employees, so that it is only in respect of 20 per cent of holiday pay that super-priority may arguably arise. However, as Mr Smith pointed out, whether this is practical in any given case will depend on factors such as whether employees are paid weekly or monthly, the timing of the next payroll, and the availability of email and similar links with employees. We can see that there may be good reasons of policy for excluding action restricted to implementation of the Scheme from the scope of "adoption" under paragraph 99, but such exclusion cannot be accommodated under the law as it stands.