

SUMMARY

## **<strong>2015/54 From which date does interest start to run on wages owed following invalid dismissal? (SK) </strong>**

***&lt;p&gt;&lt;em&gt;The Slovak Labour Code is silent on interest for late payment of wage compensation in the event an employment contract is terminated invalidly. The Civil Code provides that interest is owed in the event of late payment, but whether the relevant provisions of Civil Code apply to employment relationships is disputed. This has led to heated debate amongst Slovak scholars and to contrasting judgments (including between the Supreme Court and the Constitutional Court) on the date from which to calculate interest. Does the interest accumulate from the end of each month on which salary&nbsp; should have been paid or does it not begin to accumulate until the court has ordered the employer to pay compensation?&lt;/em&gt;&lt;/p&gt;***

### **Summary**

The Slovak Labour Code is silent on interest for late payment of wage compensation in the event an employment contract is terminated invalidly. The Civil Code provides that interest is owed in the event of late payment, but whether the relevant provisions of Civil Code apply to employment relationships is disputed. This has led to heated debate amongst Slovak scholars and to contrasting judgments (including between the Supreme Court and the Constitutional Court) on the date from which to calculate interest. Does the interest accumulate from the end of each month on which salary should have been paid or does it not begin to accumulate until

the court has ordered the employer to pay compensation?

The answer depends on whether the court order is seen as "declaratory" or "constitutive".

### **Slovak law**

An employee dismissed with immediate effect may apply to the court to have the dismissal nullified on the grounds that the employer had no valid legal reason to dismiss him or her. If the court nullifies the dismissal, the employment relationship is deemed not to have been terminated validly and it therefore continues into the future (unless the court determines otherwise). In such a case, the court will order the employer to pay the employee 'wage compensation' covering the period between (i) the date on which the employee protests, claims further employment and demands continued payment of salary and (ii) the date of the court judgment. It has been common ground that the employer owes interest on the amount it is ordered to pay based on application (by analogy) of the Civil Code by Slovak courts. However, this approach has recently been challenged by legal scholars, who believe the courts err in applying the Civil Code rules for interest on late payment. Moreover, the law is unclear on when this interest would start to accumulate. Is it from the date each month's salary should have been paid or from the date of the court order? The difference can be substantial, as illustrated by the following hypothetical example.

Let us suppose that employee X is dismissed invalidly on 1 January 2014, that he protests and demands continued payment that same day, that his monthly salary of 100 was due on the last day of each month, that on 1 January 2015 the employer is ordered to pay him wage compensation for the year 2014 and that the employer complies with that order that same day. At present, the statutory interest for late payment in this type of case is 5.05% per year. Under the "declaratory" doctrine (see below), the employer would need to pay a principal sum of 12x 100 plus the following interest:

$100 \times 5.05\% \times 11\text{months}$  (interest on January salary, February - December);

$100 \times 5.05\% \times 10\text{ months}$  (interest on February salary, March - December);

$100 \times 5.05\% \times 9\text{ months}$  (interest on March salary, April - December);

$100 \times 5.05\% \times 8\text{ months}$ , etc

The total amount of interest is approximately € 28. In comparison with the principal sum of € 1,200 this may not seem much, but the period between dismissal and judgment can be much longer than one year and in the recent past the interest was much higher: up to 15%.

Under the “constitutive” doctrine, the employer in this example would not need to pay any interest.

### **Facts**

The plaintiff was dismissed with immediate effect. He protested and demanded continued employment and continued payment of salary. As the employer did not comply, the plaintiff began court proceedings. He asked the court to order the defendant to pay him an amount equal to (i) the salary he would have been paid each month had he not been dismissed; plus (ii) interest calculated as per the “declaratory” doctrine, i.e. to be provided with interest accumulated from the end of each month on which salary should have been paid. This case report does not deal with the dismissal aspect of the case.

The court of first instance, adopting a declaratory approach, ruled in favour of the plaintiff. The appellate court, favouring the constitutive theory, overturned the judgment. It held that wage compensation in the event of an invalid dismissal is distinct from salary. Salary is owed in consideration of work performed, whereas wage compensation serves two purposes: it is a sanction imposed on the employer for dismissing someone without good reason and it compensates the employee for this breach of contract. Therefore, the right to the compensation (and, consequently, interest) does not come into being until the court has ordered the employer to pay it. The court order, as it were, creates (constitutes) the right to the compensation. In legal terms, the order is constitutive.

The plaintiff took the matter to the Supreme Court.

### **Judgment**

The Supreme Court began by establishing that the basis for the claim was the invalidity of the dismissal. To be able to claim wage compensation, the employee must inform the employer that he or she insists on continued payment of salary. Provided the court declares the dismissal invalid, it is this notice that creates the entitlement to wage compensation. All the court’s judgment does is to declare that the entitlement exists, hence the term ‘declaratory’. Thus, the plaintiff prevailed in the end.

In its judgment, the Supreme Court referenced EU law in general, observing that its decision is in full accordance with generally binding EU legislation as published in the Official Journal of

the European Union. The court may have had Directive 2011/7 on combatting late payment in commercial transactions in mind. This directive was transposed into Slovak civil law and the court used this civil law regulation by analogy in this case. The directive provides that “the creditor is entitled to interest for late payment from the day following the date or end of the period for payment fixed in the contract”.

The Supreme Court went on to instruct the lower courts to see its judgment as a binding precedent, even though the case in question was decided under the old Labour Code, which was replaced on 1 April 2002.

### **Commentary**

The issue of interest on late payment of wage compensation may appear to be a simple legal question, but it is more than that. It is highly questionable whether general civil law may be applied to labour relationships by analogy. Slovak law is not specific enough to ensure employees are provided with interest on late payment when it comes to wage compensation. However, in practice the courts grant them wage compensation including interest on late payment in any event.

Yet even following this Supreme Court ruling the legal basis for this practice is not solid. On the one hand, there is this judgment of Supreme Court stating that interest must be granted to employees. On the other, the Constitutional Court in other cases has been more hesitant. It has held that the purpose of wage compensation in cases of invalid termination of the employment contract is to satisfy the needs of the employee and to sanction the employer. In the Constitutional Court’s view, the amount of wage compensation is created de facto from the wage compensation itself, plus interest on late payment of that compensation. Even though the claims for wage compensation and interest are seen as separate claims, altogether they constitute one remedy for the employee. In the Constitutional Court’s reasoning, the main role of the courts when deciding these cases is to evaluate all the subjective and objective circumstances of the case. After assessing the evidence submitted by the parties, the court must impose a sanction on the employer that is equitable, justifiable and fair, at the same time as being a fair remedy for the employee.

In our opinion, the principal issue in this case is the difference between the declarative and constitutive approaches of the courts. The declarative approach punishes the employer more harshly than the constitutive approach. Some court proceedings concerning claims of unfair dismissal last more than four years. That means that the amount of interest on late payment can become excessive. If the court grants the employee wage compensation for four years of employment plus four years’ interest on late payment, this would be a harsh outcome for the

employer. Yet, just such a situation arises in many cases, as the courts prefer to take this approach.

In our view, the court's judgment has a constitutive effect. The court considers the employment termination and determines whether it is valid or invalid. This means that the court 'creates' the employee's claim. In cases where court proceedings take many years, the employer may be obliged to pay an excessive amount of interest. Obviously cases that last a long time are also detrimental to the employee, who has to wait several years to get justice, during which time he or she is not paid salary. The employee also loses the advantage of a long-term employment relationship, including bonuses and the possibility of promotion and salary increases. Normally, there is no option but to look for another job. In the end, however, the sanction against the employer should be equitable, justifiable and fair. Therefore, we think that the interest on late payment should be calculated from the date of the court's decision.

### **Comments from other jurisdictions**

*The Netherlands (Peter Vas Nunes):* If I understand the authors of this case report correctly, their argument is that the declaratory doctrine is harsh on employers because courts are slow and that, in combination with a high interest rate, this leads to excessive interest awards. If this is indeed seen to be unfair, why is the interest rate so much higher than the going market rate? Is the reason, perhaps, that the legislator wishes to compensate invalidly dismissed employees and employees who do not get paid on time for the serious hardship this can cause them to suffer? An employee who has been dismissed invalidly has no income for as long as the court has not ruled on the (in)validity. At present, the inflation rate is low, but suppose it goes back up to 10%. Then if the employee gets his salary four years later, he will have lost over 40% of his salary. Actually more, because if he had not been dismissed he would probably have received wage increases and maybe promotion, etc.

How different the situation in Slovakia is from that in The Netherlands. There, if a dismissal is held to be invalid, the employer must not only retain the employee but also pay him (i) salary and benefits for the intervening period, (ii) a penalty of up to 50% on top of the arrears in salary and (iii) statutory interest (currently 3%) on the total (as well as compensation for the employee's legal expenses). On the other hand, courts do not take four years to adjudicate a dismissal dispute, more like four months (or 3-4 weeks if the employee applies for temporary relief).

*Subject: Interest on late wage payment.*

*Parties: P.P. – v – T.U*

*Court: Najvyšší súd Slovenskej republiky (Supreme Court of the Slovak Republic)*

*Date: 30 April 2012*

*Case number: 6 Cdo 246/2010*

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**Creator:** Najvyšší súd Slovenskej republiky (Supreme Court of the Slovak Republic)

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