SUMMARY

2013/50 Did a beauty parlour retain its identity? (LU)

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Facts

The plaintiff in this case was a beautician. She was employed by a small limited liability company (the "Transferor") that operated a beauty parlour in rented premises. The owner of the company worked there herself along with two or three other beauticians, including the plaintiff. The plaintiff called in sick on 26 April 2010 and remained unable to perform her work until 13 October. During her absence, her employer had entered into a contract with a third party (the "Transferee") under which the Transferee took over:

the lease of the premises as from 1 September 20101;

the ownership of the furniture, equipment and stock;
the rights and obligations of the running contracts for electricity, water, telephone and insurance;
the obligation to provide free treatments to customers who had purchased pre-paid "subscriptions";
the right to use the beauty parlour's brand name (although the Transferee decided not to use this name, preferring to re-name the beauty parlour).

The contract did not provide for the take-over of the Transferor's staff, who the Transferor therefore retained as its employees[2].

When the plaintiff returned from her sick leave, the Transferor dismissed her. The plaintiff brought legal proceedings against both the Transferor and Transferee, claiming compensation for unfair dismissal. The court of first instance rejected the claim. In the case against the Transferee it reasoned that there had been no transfer of undertaking, given that the Transferee had taken over neither staff nor clientele. In the case against the Transferor, the court reasoned that the plaintiff's sick leave and the inconvenience it had caused were fair grounds for dismissal.

The plaintiff appealed.

Judgment

The Court of Appeal recalled the principle laid down in Article L.127-2 of the Labour Code according to which the transfer of an undertaking is defined as the transfer of "*an economic entity which retains its identity, and constitutes an organised grouping of resources, in particular personnel and tangible assets, allowing the pursuit of an economic activity, whether or not that activity is central or ancillary*". In order to determine whether the conditions relating to a transfer of undertaking were met, the Court of Appeal based its reasoning on the European Court of Justice's guidelines.

European case law has consistently ruled that: "*it is necessary to consider all the facts characterizing the transaction in question, including the type of undertaking or business, whether or not the business' tangible assets, such as buildings and movable property, are transferred, the value of its intangible assets at the time of the transfer, whether or not the majority of its employees are taken over by the new employer, whether or not its customers are transferred and the degree of similarity between the activities carried on before and after the transfer and the period, if any, for which those activities were suspended*" (Case 24/85 of 18 March 1986, Spijkers).

In order to refute the transfer of undertaking, the Transferee held that the identity of the

company had changed. First, the Transferee argued that a change of brand and staff had occurred. In fact, the Transferee was a single-member company as it was run by a beautician who wanted to operate alone. Moreover, there was no continuation of the same activity because the clientele had disappeared because of sporadic closing caused by the absence of the two beauticians who had worked for the Transferor.

The Court of Appeal rejected all these arguments. For the Court, if the human resources had changed, this change was only because of a violation of the legal provisions on the transfer of undertaking, in other words, the Transferee's refusal to take over the staff of the Transferor. The rules on transfer of undertakings of undertakings are underpinned by public order concerns and for those reasons the taking over of the employment contracts applies automatically by operation of law. No exception to the rules may be agreed between the Transferor and the Transferee. The change of brand was merely a secondary consideration for the Court and did not set aside the application of the legal provisions on transfer of undertakings. In addition, the transfer of the subscription agreements showed that there was no termination of the activity, so the argument that the activity had stopped could not be accepted.

The Court of Appeal noted that the material assets had been taken over and deduced from this and from the continuation of the subscription agreements with former clients that the Transferee had taken over the same activity at the same place as the Transferor. A transfer of undertaking between the two companies was therefore deemed to have occurred in the present case. Consequently, the Court of Appeal overturned the judgment of the Labour Court of Luxembourg, which had rejected the claim of the employee for unfair dismissal, declared the claim against the Transferee admissible and referred the case back to the first instance court (but with different judges).

Commentary

This case illustrates the important but complex issue of how to determine whether an undertaking maintains its identity when no agreement is made to transfer the employees. In this context, the Court of Appeal tried to apply European Court of Justice case law in the field of transfer of undertakings, according to which the national jurisdiction must apply the technique of bundling evidence ("*faisceau d'indices*") in order to assess whether a transfer occurs. To this end, the judge must identify all the assets or means that have been taken over and then make an overall assessment as to whether there is a transfer. In the present case, the Court of Appeal considered that the transfer was mainly characterised by the transfer of the lease agreement, the subscriptions and the material assets. According to the Court, this was sufficient for the rules on transfer of undertakings to apply. This suggests that the Court, in its

overall assessment, decided to allow the transfer of the material assets to prevail over the lack of any evident transfer of staff - as, in this case, there had been no intention to take over the staff. But one might question whether the mere fact that the material assets were transferred adds up to a transfer of the undertaking.

It is unfortunate that the Court of Appeal did not examine the question of the transfer of staff in more depth. It is true that the transfer of staff should not depend on any agreement between the Transferor and the Transferee that may be concluded to avoid the application of the rules. However, the judge ought perhaps to have looked at the bigger picture, which involves assessing the relative importance of material assets and human resources and determining which of these means of production was decisive for the business in question.

In our opinion, it is not clear whether material assets are a determining factor for the successful running of a beauty shop. To be a beautician requires technical knowledge and is included in the list of skilled professions in Luxembourg. It is therefore uncertain whether the material assets and/or the premises are more important than the staff for the business of a beauty shop.

In this context, the change of brand could indicate that the clientele were not bound to the brand, as would be the case, for example, with a franchise. This would support the view that personal relations with clients were more important to the business than the location or value of the material assets and consequently that the staff were essential in this particular case. The Court of Appeal unfortunately failed to conduct this kind of market analysis. If it had done so, this could well have led to the conclusion that no transfer had occurred, as the determinant production means - i.e. the staff - had not transferred.

The decision shows the difficulty that national courts have in applying the methodology established by the European Court of Justice for transfer of undertakings. It is perhaps optimistic to expect the employment courts to go through a market analysis of the business in each case. In practice, therefore, the courts limit themselves to what we could call an "*appearance*" of transfer, inspired by analogous cases, instead of looking for legal criteria.

Finally, we need to consider the practical implications of the decision. In this case, the Transferee considered that she had no need to take over the former employees because she wanted to exercise the activity alone and was fully qualified to do so. The precedent set by this case could have a negative effect on the transfer of commercial leases. It is noteable that, on the date of the judgment, the Transferor and the Transferee were both in bankruptcy and represented by their respective liquidators. The failure of both businesses during the proceedings suggests that the Transferee's argument that the Transferor's previous activity

had ceased, might have needed more consideration. In the context of the economic downturn, one might argue that applying the transfer of undertaking provisions to small businesses and singlemember companies such as in this case is inappropriate.

Comments from other jurisdictions

Austria (Daniela Krömer): In general, Austrian Courts can be credited with giving thorough attention to the specifics of the business, the importance of material and immaterial assets and the know-how of personnel, when determining whether or not a transfer has taken place. A good example would be the Supreme Court's judgment on the transfer of a unit in charge of acquiring advertisements for phone books (8 ObA 143/98g), in which the nature of the business and the value of immaterial assets (contact details as know-how) was thoroughly assessed. In that case, specific attention was given to the transferee's intention to take over some of the transferor's employees, as this gave a strong indication that the transferee was interested in taking over the immaterial assets – the contact details – of the undertaking. Had the staff not been partially taken over, no transfer of the undertaking would have taken place. Therefore, it is very likely that Austrian Courts would have assessed the importance of the personnel in a beauty shop in terms of its identity if faced with a similar situation - assuming of course that the lawyers representing the case provide adequate information.

Germany (Paul Schreiner): In Germany a court would probably have ruled the same way as the Luxembourg court did. The reasoning, however, would probably have been different. The German courts tend to differentiate between different types of businesses, taking into account the importance of human resources to the activity in comparison with the material assets.

However, even if a German court found that human resources outweighed the importance of the material assets, this does not mean that the non-take-over of the employees by contract excludes a transfer of undertaking per se. The intended transfer of employment is just one of many arguments regarding whether a transfer took place. In the case at hand, I think the decisive criterion might have been the taking over of the client subscriptions. To generate income from the beautician business, one needs specialized human resources on the one hand, but also a connection with clients on the other. The generation of income depends on both aspects and so the contractual transfer of one of these constitutes a transfer of the undertaking.

Slovenia (Petra Smolnikar / Nives Slemenjak): With the transposition of Directive 2001/23/EC into Slovenian legislation, the automatic transfer of employment relationships from transferor to transferee is deemed to occur as a result of a legal transfer of an undertaking or a part thereof taking place. This includes, *inter alia*, any transfer based on a sale and purchase

agreement, a lease agreement, an agreement on the transfer of rendering services, etc., including a transfer not based on a (written) contractual relationship. Slovenian courts frequently consider the criteria set in the *Spijkers* case when ascertaining the rights of employees following a (legal) transfer.

As the ECJ's case law aims at giving greater importance to the broader "economic entity" aspect of a transfer (including the importance of transferring staff) as compared to the mere "conduct of the same activity" aspect (where performance of the same or a similar activity suffices for the conclusion of an automatic transfer), we agree with the view that in cases such as the present one, the human resources impact on the economic independence of a business activity should be assessed in relation to the overall transfer that took place.

In Slovenia beauticians need to attain a certain level of technical education to enable them to work or operate a beauty shop, meaning that this kind of business activity cannot survive without adequate personnel propelling it. However, in our view, the mere transfer of staff should very rarely be the decisive factor as to whether a transfer occurs or not, as this might very well subvert the aims of the Directive.

The staff factor should play an even lesser role where there is a clear transfer of business components, indicating that an economic unit as a whole has been transferred. In this case the relevant factors included: (i) the subscription agreements connecting the existing clients to the beauty shop; (ii) the premises, which must have been known in the neighbourhood as a beauty shop, connecting existing and potentially new clientele to the beauty shop; (iii) the tools, furniture and equipment necessary for the immediate commencement and continuation of the business; (iv) infrastructure related to the premises and the activity; and (v) the brand – despite it being changed afterwards, which is a future business decision of the Transferee.

In addition, the Transferee in this case apparently held the necessary beautician licences and technical knowledge to enable it to operate after the transfer. Thus, the transferred unit was clearly able to operate independently, despite lacking the Transferor's staff. The fact that the staff did not transfer was only because of the terms of the agreement between the Transferor and Transferee, which, we believe, represents a clear violation of employee's rights under the Slovenian Employment Relationship Act.

United Kingdom (Bethan Carney): The Employment Appeal Tribunal in the UK has held that the question of whether there has been a transfer should be split into two parts and the tribunal should first consider whether or not there is an undertaking and, then, whether that undertaking has transferred (*Cheesman and Ors* - v - *R Brewer Contracts Ltd* 2001 IRLR 144). For there to be an undertaking there must be 'a stable economic entity, which is an organised

grouping of persons and of assets enabling (or facilitating) the exercise of an economic activity that pursues a specific objective'. There is little doubt that in the present case a UK court would have found that there was an undertaking comprising employees, premises, tools, furniture, equipment, stock, utilities, goodwill and clients. For there to be a transfer, this economic entity must retain its identity in the hands of the transferee. This question is one of fact for the tribunal, which must consider all the circumstances. In *Cheesman*, the EAT reiterated the European law position that 'the decisive criterion for establishing the existence of a transfer is whether the entity in question retains its identity, as indicated, among other things, by the fact that its operation is actually continued or resumed'. In the UK, as in Luxembourg, the type of business should be considered when trying to determine whether or not the non-transfer of the employees was determinative. However, in practice, UK courts have generally been willing to find that there has been a transfer and in these circumstances, where there is essentially the transfer of a business (premises, stock, utilities, tools and equipment all transferred and the type of activity carried out by transferor and transferee was the same), it is likely that UK courts would also have deemed it to be a transfer of an undertaking. There is no exemption for small businesses in the UK.

Creator: Cour d'appel (Court of Appeal)
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Case number: 38327