SUMMARY

2012/58 Employer cannot assign claim against employee to third party (CZ)

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Facts

The defendants in this case (the 'Defendants') were the Managing Director and the CFO of a joint stock company (the 'Company')[1]. They were responsible for a decision by the Company to loan approximately

€800,000 to another company. That other company failed to repay the loan. The Company held the Defendants liable for the loss to the Company. The Defendants denied liability, whereupon the Company - represented by a new Board of Directors - brought proceedings in which it claimed the maximum sums for which under Czech law employees can be held liable for damages caused to their employer, which is 4.5 times their average monthly salary. In the case of the Managing Director this was € 32,650 and in the case of the CFO this was € 11,384. The claim was based on the contention that the Defendants had breached their duty of care towards the Company, in particular by failing to investigate the debtor's creditworthiness and by accepting as security for the loan a pledge that proved to be invalid.

The courts of first and second instance ordered the Defendants to pay, but on further appeal the Supreme Court reversed their judgments and remanded the case back to the court of first

instance.

While the case was pending (again) in the court of first instance, the Company assigned its claim against the Defendants to a third party (the 'Assignee'). The Defendants argued that such an assignment was not possible. The court of first instance dismissed this argument. On appeal, however, the assignment was held to be invalid (and, as a result, the court did not allow a change of plaintiff) on the ground (inter alia) that Czech employment law does not allow an employment-related claim to be assigned. The Company appealed to the Supreme Court.

Judgment

The Supreme Court held that rights and duties arising out of an employment relationship cannot be transferred unless the law explicitly allows such a transfer, such as in the case of the transfer of an undertaking. An agreement between an employer and a third party is an insufficient basis for the transfer of a claim. This meant that the assignment of the claims vis-à-vis the CFO was invalid.

As for the Managing Director, the question was whether he qualified as an employee and, hence, whether the rules of employment law applied to his situation. The Defendant in question had two distinct capacities: that of employee and that of chairman of the Board of Directors (i.e. a corporate capacity). Under Czech law, however, a member of a Board of Directors cannot simultaneously be an employee to the extent that his work as an employee is of a managerial nature (business management).

The Supreme Court remanded the case back to the court of first instance, which was instructed to decide (for the third time!) on the liability issue and on that of the Managing Director's employment status.

Commentary

Czech law on transfer of undertakings is based on Directive 2001/23. However, Czech law has gone further than required by the Directive, by providing that any transfer of an employer's tasks and activities (or a part thereof) qualifies as a transfer of undertaking and therefore leads to the assignment of rights and obligations. Under the Labour Code, a transfer of rights or obligations arising out of an employment relationship is possible only if the conditions for a transfer of undertaking are met. In other words, the rights and obligations between an employer and employee can only be assigned within the framework of a transfer of undertaking and in that event, they must all be assigned - individual rights cannot be transferred.

It may be noted that, as regards the assignment, this judgment was based on the law in force as of 20 November 2007 (the date on which the assignment agreement was concluded). The Labour Code was amended on 1 January 2012 and now provides explicitly that employment-related claims cannot be assigned.

The Supreme Court's judgment also deals with a classic issue under Czech law, namely whether a person can simultaneously be an employee and a board member (or an executive in a limited liability company). The Supreme Court has repeatedly held that this is not possible to the extent that the directorship duties overlap with the job description under the employment agreement, and that therefore an employment agreement in such a situation is invalid (unless a special procedure, introduced in 2012 and not relevant here, is followed).

An example of a situation where there is no overlap would be where a board member is also a cleaner in the company. An example where there is overlap would be where a board member is also the company's CEO or CFO. Clearly, there is a grey area in between these extreme examples. The rationale for not allowing overlap has to do with liability. A board member is liable for breach of his or her obligations without limitation, whereas the liability of an employee for such a breach is limited (with certain exceptions, such as intentionally caused damage). In addition, in certain situations a board member may be held personally liable for company liabilities.

In the event the courts in the pending case hold that the Managing Director was not validly employed, (i) the assignment of the claim against him was valid; (ii) his potential liability is not limited to 4.5 times his average monthly salary[2]; and (iii) he will need to prove that, as a board member, he acted with the required level of care.

Comments from other jurisdictions

Austria (Martin Risak): The decision touches on two questions which I shall answer briefly against the Austrian background. The first concerns the employee status of directors. The prevailing opinion in Austria holds that one has to distinguish between the two different types of capital companies. Members of the managing board (Vorstand) of a joint stock company (Aktiengesellschaft) are not considered to be employees, as the relevant Act provides that they are not subject to directives of the supervisory board (Aufsichtsrat), and have only to act in the best interest of the company. As being subject to the employer's direction and orders is an essential element of the status of an employee, members of the managing board are not considered as employees but as working under a free service contract. On the other hand, directors of a limited liability company (Gesellschaft mit beschränkter Haftung) are deemed to be employees, as the relevant statutory provisions make them subject

to directives of the shareholders. The only exception is where they are shareholders themselves and have the power to influence decisions made in shareholders' meetings (i.e. if they hold a majority of the shares or have a vetoing minority). In such a case, they are not subject to any directives, other than those given by themselves.

The second question raised regards the legality of assigning a claim against an employee to a third party. As there are no special rules in this area, the general rules of contract law apply. The assignment does not need the consent of the debtor as his or her situation does not change at all except for a change to the identity of the creditor. He or she may use all the objections used against the claim of the former creditor.

Finland (Johanna Ellonen): The question of whether a person can be simultaneously an employee and a member of the board has not caused particular concern in Finland as such persons are, as a rule, considered employees and covered by employment legislation. However, it is likely that not all employment legislation applies to them, e.g. the Finnish Working Hours Act (1996/605) and collective bargaining agreements often exclude corporate management from their scope. In their duties as board members they must act according to the Finnish Companies Act (2006/624). However, the status of managing directors of limited liability companies has been subject to some debate, although currently it is clear from case law that managing directors of limited liability companies are not considered to be employees but as statutory corporate organs to whom employment legislation does not apply.

However, if an employee acts simultaneously as an employee and a board member, this could be problematic, for example in relation to liability for damages. Both the Finnish Companies Act and the Employment Contracts Act contain provisions regarding liability for harm caused, the liability under Employment Contracts Act being more restricted. Legal scholars generally consider that employees can be held liable under the Companies Act for damages caused in their duties as board members, although there are no explicit provisions in the Act about this. Evaluating whether the harm has been caused by the individual in his or her role as a board member or an employee may, however, prove difficult in practice.

As regards the issue of assigning/selling employment-related claims to third parties, the Finnish Employment Contracts Act expressly prohibits the assignment of obligations arising from employment relationships to third parties without the other party's consent, unless the claim has fallen due. Even if such assignments were possible (e.g. with the managing director), they are not typical in Finland in employment or service relationship-related matters.

Luxembourg (Michel Molitor): Under Luxembourg law, an assignment can involve the transfer of any actions or rights subject to terms or conditions or related to a future right. Thus, there is

no obstacle to assigning a claim about the misconduct of a managing director. Nor is there any to prevent the assignment of claims relating to an employment contract and to the best of our knowledge, there is no particular case law in Luxembourg preventing an employer from assigning a claim against one of its employees to a third party. However, we can imagine that the Luxembourg Courts could be against such an assignment, as in the present case. It is uncertain whether the Labour Courts would accept jurisdiction over such an assignment and it is even harder to imagine another court accepting jurisdiction.

However, the assignment of a claim from an employment contract is only conceivable in cases in which there has been an intentional tort or gross negligence pursuant to Article L.121-9 of the Labour Code. In terms of a claim against a managing director, there is no restriction, since a managing director is liable towards the company for harm arising from any infringement of the Law of 1915 on commercial companies and for any misconduct in the management of the company's affairs, in other words, any kind of fault.

Therefore, in the matter at issue, the solution in Luxembourg law would depend on whether the fault related to the functions of the managing director or to employment activities. In Luxembourg it is possible to be both a managing director and employee, but only on condition that the positions are kept separate.

The Netherlands (Peter Vas Nunes): The legal status of an employee who is also a member of his employer's Board of Directors (an 'Employee- Director') has been the subject of considerable debate among Dutch scholars and in case law, such an employee having two capacities simultaneously: (i) he or she is an employee, to whom the normal rules of employment law apply, with one major exception, namely that, in contrast to all other employees, an Employee-Director can be dismissed without the employer needing to obtain a dismissal permit and (ii) he has a corporate capacity, with power to represent the company, to whom the rules of company law apply, including the rule that a Director can be dismissed 'at any time'. Until 1992, it was widely held that the corporate capacity overruled the employment capacity and that, therefore, the principle that a Director can be dismissed at any time trumped, for example, the rule of employment law that an employee cannot be dismissed during (the first two years of) sickness. In that year, in the Levison case, the Supreme Court held that an Employee-Director who is dismissed during sickness loses his corporate capacity but not his capacity as an employee. In 2005, the Supreme Court, while retaining this doctrine, stressed that the two capacities of an Employee-Directorcannot be separated except in two cases: (i) where such an individual is dismissed during sickness (and similar situations where a dismissal prohibition applies) and (ii) where the parties have agreed explicitly to separate the two capacities. The status of an Employee-Director remains complicated.

An ironic detail is that, as from 1 January 2013, Directors of companies listed on a stock exchange will no longer have the status of an employee, but it is anticipated that some of these Directors may negotiate contracts that are governed by the rules of employment law. I know of only one instance (District Court of Rotterdam 12 February 2008, LJN:BC6356) where an employer assigned to a third party a claim it had against one of its employees. The case concerned an employee who had defrauded one of his employer's clients. The client had a claim against the employee. The employer purchased this claim and proceeded to sue the employee. The issue of whether such a purchase (resulting in an assignment) was legally possible on employment- related grounds was not even raised and the court awarded the claim. It is very rare for an employer to have a claim against an employee. Employees are almost never liable for damage they cause to their employer with the possible exception of speeding and parking tickets charged to the employer (usually via the car lease company). Employees are occasionally ordered to repay salary that was paid erroneously. But why would an employer want to sell or assign such a claim to a third party? In brief, there is almost no legal precedent on this subject in The Netherlands.

Footnotes

1 Czech company law distinguishes two types of corporation: a joint stock company, which is comparable to a German AG, a British Plc or a French SA, and a limited liability company, that is comparable to a German GmbH, a British Ltd or a French Sàrl. A joint stock company is managed by a Board of Directors. A limited liability company is managed by one or more 'executives'.

2 The Company could only claim damages by extending the claim filed with the court or by filing a new claim; yet, as the events date back to 1998, a claim in excess of 4.5 times his average monthly salary would be statute-barred.

Subject: Miscellaneous

Parties: CEPRO, a.s. - v – Ing. K.F. and Ing. H.D.

Court: Nejvyšši soud Ceské republiky (Supreme Court)

Date: 6 September 2012

Case Number: 21 Cdo 786/2011

Publication: www.nsoud.cz > http://www.nsoud.cz/Judikatura/judikatura_ns.nsf/WebSearch/8CA60E1D8A96D795C1257A79004629E1?openDocument&Highlight=0,

EELA EUROPEAN EMPLOYMENT LAWYERS ASSOCIATION

Creator: Nejvyšší soud (Czech Supreme Court)
Verdict at: 2012-09-06
Case number: 21 Cdo 786/2011