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The non-competition duties of a dismissed employee exempted from work during the notice period (LU)

CONTRIBUTORS Michel Molitor and Régis Muller*

Summary

The Luxembourg Court of Appeal (*Cour d'appel de Luxembourg*) confirmed that an employee dismissed with notice and exempted from performing their work during the notice period is no longer bound by the non-competition duties arising from their loyalty obligation and can therefore engage in an employment contract with a direct competitor of their former employer during that exempted notice period. However, the Court of Appeal decided that, even if the former employee is in principle entitled to use the know-how and knowledge they acquired with their former employer, the poaching of clients during the notice period must, due to the facts and circumstances and in the light of the rules applicable in the financial sector, be considered as an unfair competition act and therefore constitutes serious misconduct justifying the termination of the employment contract with immediate effect.

Facts

A person had been employed by a company in the Luxembourg financial sector as 'Client Advisor' since 1 March 2001, under an employment contract dated 27 December 2000.

At the end of 2015, facing economic difficulties, the employer decided to review the remuneration of its 'Client Advisors'. In this context, on 29 February 2016, the employer submitted to the employee a new employment contract with a lower monthly remuneration. The employee refused to sign the contract. aAs a consequence, and on the basis of these economic difficulties, the employer dismissed the employee with a notice period of six months starting on 1 March 2016 and ending on 31 August 2016. The employer exempted the employee from performing their work during that period.

On 4 March 2016, the employee signed a new employment contract with a direct competitor of the employer, effective from15 March 2016.

On 28 April 2016, the employer dismissed the employee with immediate effect for serious misconduct during the notice period. In the dismissal letter, the employer accused the employee of serious misconduct consisting of a breach of the duty of loyalty during the notice period (conclusion of a new employment contract with a competitor, unauthorised contact with clients and poaching of clients) and unfair competition acts contrary to their obligation of confidentiality and in violation of the rules of conduct of the financial sector issued by the Luxembourg supervisory authority (the 'CSSF', i.e. *Commission de Surveillance du Secteur Financier*).

The employee filed a lawsuit against the employer and claimed damages for unfair dismissal regarding both the termination with notice and the termination with immediate effect.

The first instance judges, namely the Labour Court of Luxembourg (*Tribunal du travail de Luxembourg*), decided that both the dismissal with notice and the dismissal with immediate effect were justified and valid. The employee then lodged an appeal against this judgment with the Luxembourg Court of Appeal.

Judgment

Although the decision of the Luxembourg Court of Appeal confirmed the validity of both the dismissal with immediate effect and the dismissal with notice, the decision is particularly interesting regarding the dismissal with immediate effect during the notice period, especially the extent of the loyalty obligations, and more specifically the non-competition duties of an employee during the employment relationship.

Regarding the dismissal with notice, which was based on economic reasons, the Court of Appeal confirmed that such dismissal was valid as the employer had demonstrated that financial difficulties existed and the offering

* Michel Molitor is the managing partner of MOLITOR Avocats à la Cour SARL in Luxembourg, www.molitorlegal.lu. Régis Muller is partner within the Employment, Pension & Immigration department of MOLITOR Avocats à la Cour SARL in Luxembourg, www.molitorlegal.lu.

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of a new employment contract to the employee was not inconsistent in this context, as it was for a lower salary and for the purpose of retaining clients.

An employee cannot be prohibited from taking a new employment during the exempted notice period

On this point, the decision of the Court of Appeal differs from the position of the first instance judges. The Labour Court of Luxembourg (first instance) decided that the employee was in breach of a contractual provision, namely Clause 9 of their employment contract under which the employee was not authorised (i) to perform for their own account, directly or indirectly, an activity similar or competitive to the activities of the employer, and (ii) to accept another remunerated job during the employment relationship.

In the Court of Appeal, the employee argued that Clause 9 of the employment contract was null and void as the provisions of Article L. 124-9 (1) of the Luxembourg Labour Code, which allow an employee exempted from performing work during the notice period to enter into a new employment relationship with a new employer,[1] are of public order, so that the parties cannot derogate from such provisions by contractual agreement.

The Court of Appeal did not follow any of the above arguments. It noted that the provisions of Clause 9 of the employment contract were not inconsistent with the provisions of Article L. 124-9 (1) of the Luxembourg Labour Code, as the contractual provisions did not prohibit the employee from being hired by a new employer during the exempted notice period, even if it was a direct competitor of the employer.[2]

The Court of Appeal further pointed out that:

- even in the absence of specific provisions in the employment contract, the employee is for the whole duration of the employment contract, automatically and by the effect of the law, bound by non-competition duties prohibiting them from developing a professional competing activity for their own benefit or for the benefit of a third party; and
- while the rights and duties of the parties during the notice period remain unchanged, including regarding non-competition, this is no longer the case in the event of an exemption from work during the notice period: in this case, the non-competition duties automatically cease to apply.

As a consequence, and unlike the first instance judges, the Court of Appeal decided that the contractual provisions of Clause 9 of the employment contract were not null and void, but that the employee did not breach those provisions by entering into a new relationship with a direct competitor of the employer during the exempted notice period.

Breach of the confidentiality and loyalty duties of the employee

The Court of Appeal confirmed the decision of the Labour Court on this point.

According to the Court of Appeal, the general principle of good faith in the performance of contracts,[3] which is also applicable to employment contracts, has a particular meaning in labour law and is not limited to an obligation to refrain from competing with the employer, it being also a question of the respect of ethical behaviour.

The Court of Appeal therefore confirmed the position of the Labour Court, namely that an employee:

- is in principle entitled to use the know-how and knowledge they acquired with their former employer, provided they refrain from unfair competition acts; and
- must, for the whole duration of the employment contract, refrain from acts of actual competition with their employer.

Breach of obligations arising from the CSSF circulars

The Court of Appeal also decided that the behaviour of the employee, who was working in the financial sector, was a breach of the rules of conduct issued by the CSSF in Circular no. 07/307 which explained and specified certain provisions of the Law of 13 July 2007 on markets in financial instruments, implementing Directive 2004/39/EC (the 'MIFID' Directive)[4] and in particular the following Articles:

- Article 140 under which a financial institution "shall refrain from luring away or attempting to lure away clients from a competitor using unfair means. It shall not seek to obtain and use confidential information on the clients of a competitor and at the disposal of a member of its staff previously employed by this competitor. It shall also make sure that its staff does not actively use this information for the same purpose"; and
- Article 141, which states that a financial institution "shall refrain from any such practice, notably if an account manager changes the employer, in which case and depending on the circumstances, the institution and the employee concerned might be held responsible in many aspects under criminal and civil law".

The Court of Appeal concluded from the above that the employee committed serious misconduct justifying dismissal with immediate effect.

1. This Article also provides that in such an event, the former employer must pay to the employee until the end of the exempted notice period the difference between the former salary and the salary paid by the new employer, provided it is lower than the former.
2. The Court further pointed out that it was also not contradictory to (i) the mandatory legal provisions governing the post-termination non-competition clauses, and (ii) the CSSF rules regarding competition in the financial sector.
3. Article 1134 of the Luxembourg Civil Code.
4. Repealed by the Law of 30 May 2018 on markets in financial instruments, implementing Directive 2014/65/EU on markets in financial instruments ('MIFID II').

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Commentary

The decision of the Court of Appeal is interesting regarding the extent of the non-competition duties of an employee towards the employer during the employment relationship.

The Court of Appeal clearly distinguishes between the various situations during the employment relationship, namely:

- While the employee is actually performing work for the employer, even during the notice period, whether or not there is a specific clause in the employment contract regarding the non-competition duties, the employee is strictly prohibited from performing a competing activity, on their own account or for the benefit of a third party, arising from their duty of loyalty.
  According to Luxembourg case law certain preparatory acts of a future competing activity during the employment relationship (e.g. the setting-up of a company or the conclusion of a lease agreement) do not constitute a breach of the non-competition/duty of loyalty of an employee as long as they do not actually start such competing activities.
- During the notice period, an employee who is exempted from work cannot be prohibited from entering into a new employment relationship with a new employer, even if it is a direct competitor of the former employer, but must refrain from acts of unfair competition and more generally from disloyal acts vis-à-vis the former employer.
  In addition, it arises from Article L. 125-8 of the Luxembourg Labour Code relating to the post-termination non-competition clauses of an employment contract, as interpreted by Luxembourg settled case-law, which gives a strict interpretation of this Article in favour of employees, that the extent of such non-competition commitments of an employee is limited to the prohibition of running a personal undertaking with a similar or competing activity the termination of the employment contract.[5]

Therefore, under Luxembourg law, a dismissed employee who is no longer performing work for the employer cannot be prohibited from entering, as employee, into a new employment relationship with a new employer, even if this new employer is a direct competitor of the former employer. The employee must only refrain from unfair acts of competition. This is a matter of fact and at the sole discretion of the judges.

The new EU Directive on Transparent and Predictable Working Conditions, and more specifically Article 9(1) of that Directive providing that "*Member States shall ensure that an employer neither prohibits a worker from taking up employment with other employers, outside the work schedule established with that employer, nor subjects a worker to adverse treatment for doing so*", should have no impact on the Luxembourg solutions regarding the extent of the loyalty and non-competition duties of an employee during their employment relationship. This is so especially in view of Article 9(2) of the Directive providing that the Member States can authorise restrictions by employers on the basis of objective grounds such as, *inter alia,* the protection of business confidentiality or the avoidance of conflicts of interest. In addition, and despite the fact that the scope of the Directive is broad (e.g. it concerns all workers in the European Union), the provisions of Article 9 are specifically aimed at protecting workers active in new forms of work, such as workers on zero-hour contracts.[6]

Comments from other jurisdictions

Finland (Janne Nurminen, Roschier, Attorneys Ltd.): In Finland, the Employment Contracts Act (55/2001, as amended, the 'Act') includes a prohibition of competing activities during the employment relationship. An employee must not work for a competitor or engage in such activity that would, taking the nature of the work and the individual employee's position into account, cause harm to the employer and be considered as an unfair competitive act. Further, the preparations for future competing activities cannot be considered acceptable. The prohibition is valid even if the employee would have been relieved from the work obligation during the notice period.

If a similar case would take place in Finland, the employer would have the option of requesting an interim injunction so that the employee had to discontinue the competing activities as well as claim compensation for any loss caused by the employee although typically such loss is too difficult to prove. Further, it should be noted that if the employment contract was terminated with immediate effect, the prohibition of competing activities would naturally cease to apply as it is only applicable during the employment.

Germany (Andre Schüttauf, Luther Rechtsanwaltsgesellschaft mbH): Germany has a statutory non-competition clause in Section 60 of the Commercial Code ('Handelsgesetzbuch'). Even though the wording might suggest that the provision applies only to employees providing commercial services, there is no dispute that other employees are subject to the non-competition clause as well if reference is made to this provision.

In addition – as in Luxembourg – it is also recognized that, in the absence of a specific provision in the employment contract, the non-competition duties follow from the general principle of loyalty to the employer.

5. For a limited period of time, i.e. one year, and in a limited territory, i.e. the Grand-Duchy of Luxembourg.

6. Expressly mentioned in the French version of Statement 19/873 of 7 February 2019.

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In Germany employees are forbidden from competing with their employer during the whole employment relationship. The ban on competition also applies during the notice period. The exemption of the employee in principle has no impact on that obligation. In this respect, the Federal Labour Court ('Bundesarbeitsgericht') has stated in its judgement of 17 October 2012 (10 AZR 809/11) that the employer has a recognizable interest in observing the non-competition clause even if the employee is released from the obligation to perform work. A different interpretation of the statement of exemption is conceivable if the crediting of other earnings during the exemption period has expressly been declared. In these circumstances, the employee may assume that they are permitted to carry out competition activities before the end of the notice period. In the vast majority of cases, however, such crediting is not declared and does not arise from the regulations in the employment contract either. Another exception only applies, of course, if the employer waives the non-competition duties.
Nevertheless, even before the end of the employment relationship, the employee may prepare to set up their own company or to switch to a competitor. Preparatory actions which do not directly interfere with the employer's interests are permitted. However, it is forbidden to engage in advertising activities, e.g. by brokering competitive transactions or actively luring away clients or employees.
In summary, it can be said that the prohibition on poaching clients follows directly from the employee's obligation not to compete with the employer as a general principle of loyalty. Since, contrary to the decision of the Luxembourg Court of Appeal – the non-compete obligation applies during the exemption period, there is no need to refer to specific rules of conduct, e.g. in Luxembourg arising from the CSSF circulars.
Whether the violation justifies a dismissal with immediate effect depends on the individual case. The German law always weighs up the interests of both parties. The breach of the non-compete obligation in principle represents an important reason for an extraordinary termination. In concrete terms, the effectiveness of such a termination depends on the degree of guilty plea and the nature and effect of the competitive act.

Greece (Effie Mitsopoulou, KG Law Firm): Under Greek law, dismissal can take place either immediately or with notice. The only difference is in the amount of the severance due: in the first case the total amount of the legal severance must be paid, whereas in the second case only half of the legal severance is due. In case of dismissal with notice, all rights and obligations of the employment relationship remain in full effect: the employee cannot be requested not to work and stay at home (garden leave).
Therefore, there is no question of a second dismissal since during the notice period the employment agreement is still valid and in full effect.
In case of dismissal with notice, the dismissal will take place upon the lapse of the actual notice period and at such time the legal severance must be paid by the employer. Since during the notice period the employment remains valid and in effect, so will all the duties the employee is obliged to respect, namely the duty of loyalty towards their employer. Consequently during the notice period, the employee is bound by the same obligations they had before the giving of notice: they must be loyal to their employer and so will not be allowed to proceed with any competitive and similar acts, e.g. poaching of clients.
Therefore the Greek courts would have ruled *similar* to the Luxembourg Court of Appeal on the first point namely that:

> even in the absence of specific provisions in the employment contract, the employee is for the whole duration of the employment contract, automatically and by the effect of the law, bound by non-competition duties prohibiting him from developing a professional competing activity for his own benefit or for the benefit of a third party" but differently on the second point where they would have ruled instead that: "the rights and duties of the parties during the notice period remain unchanged, including regarding non-competition, since no exemption of work during the notice period applies.

Finally the post-termination non-compete clause, which can include a non-solicitation obligation as well, is usually included in the employment contract and, in order to be valid, case law has stipulated that it must include fair compensation paid to the employee for the restricted period.

United Kingdom (Richard Lister, Lewis Silkin LLP): Employee competition is an area regulated by EU law only to a very limited extent, so one would expect marked differences between European countries' laws on the remedies available to employers when faced with departing staff who are a competitive threat. From the above summary of the law in Luxembourg and the Court of Appeal's decision, it appears that employers in the UK in a comparable situation would be in a slightly stronger position to challenge and restrict an employee's activities during their notice period.
In the UK, this area is regulated by the common law of contract rather than statute. An implied 'duty of fidelity' is implied into all employment contracts, meaning that the employee must have regard to the employer's interests and serve the business loyally. This duty continues to apply fully during any notice period. It is commonplace in the UK, when an employee gives or receives notice to terminate the employment contract, for the employer to want the employee to stay away from work for all or part of the notice period. This depends on there being a contractual right to require it but, if the employer has such a right, the enforced period of absence is generally known as 'garden leave'.

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Garden leave is an effective tool for UK businesses to minimise or mitigate the damage that could be caused by the employee in question. For instance, a new executive could be brought in to manage and/or develop a particular client relationship while the departing employee is kept 'out of the market'. In combination with express post-termination restrictions in the contract, garden leave can therefore provide a means of ensuring effective protection against competitive threats on termination of employment.

Another factor in the employer's favour in the UK is the courts' willingness, in appropriate circumstances, to grant a 'springboard injunction' where a departing employee is joining a competitor. This is a discretionary remedy intended to cancel out an unfair advantage which the employee (or a competitor) may have gained as a result of the employee's breach of legal obligations – for example, their duty of fidelity or obligations in relation to confidential information. Springboard injunctions are available to prevent any future serious economic loss to an employer caused by employees taking unfair advantage of any serious breach of their employment contract. Significantly, this might include an employee taking preparatory steps to compete during the notice period, in breach of the implied duty of fidelity.

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