# Employment & Benefits - Austria

## Non-compete clauses – Supreme Court changes longstanding position

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### Introduction

For decades it was settled case law that compensating (or promising to compensate) a new hire for contractual penalties owed by the employee to his or her former competitor employer for breaching a non-compete clause amounted to anti-competitive practice and both the former employee and new employer were liable under the Unfair Competition Act.

In a landmark decision,(1) the Supreme Court reversed this case law and allowed the practice to stand, mostly citing German literature to explain its rationale.

### Facts

In Spring 2013 several employees of a chemicals company which distributed industrial chemicals terminated their employment because they were unhappy with the management style of their plaintiff employer. At about the same time, one of the employees contacted the Swiss parent company of the future defendant, inquiring whether he and his like-minded coworkers could instead work for this competing group of companies. At the time, the Swiss parent company had no interest in establishing a presence in Austria, but changed its mind when it became apparent that valuable expertise would be lost to other employers. The Swiss parent company set up an Austrian subsidiary and employed two of the plaintiff's former employees.

The defendant was also in the chemicals business. When one of the potential new hires voiced concerns that he might be in violation of a non-compete clause which prohibited him from working for a competitor for 12 months following the termination of his employment, the defendant contacted its Swiss parent company and had Swiss counsel review the non-compete clause under Austrian law. The Swiss counsel believed that the clause was overly vague and too ambiguous to be enforceable under Austrian law (the issue was whether the restriction from working 'in the areas' of the plaintiff was a geographical or functional term). Based on that opinion, the defendant wrote a letter to the future employees, indemnifying them against any claims by their former employer in connection with the alleged breach of their non-compete clauses.

The former employer filed suit and requested that the defendant (the Austrian subsidiary of the Swiss-based conglomerate) refrain from enticing away and employing its employees, including the two individuals already employed by the defendant, as they were bound by non-compete clauses. The plaintiff claimed that the defendant's aggressive enticing away of its employees by way of a guarantee to cover them against damage claims brought by the plaintiff amounted to an unfair practice and justified a temporary cease-and-desist order in order to prohibit the defendant from hiring the plaintiff's former staff until the restrictive period (12 months following the termination of employment) had lapsed.

The defendant argued that the plaintiff's former staff had approached it and not the other way around; therefore, it had not enticed anyone away. Further, the defendant claimed that it had validly relied on the

legal opinion of a reputable Swiss law firm when assessing whether to employ the plaintiff's former staff and that, in essence, bringing in lawyers to write a well-founded and reasoned legal opinion could never amount to an unfair business practice.

**Lower court rulings**

In line with the plaintiff's argument and supposedly reflecting the established case law, the first-instance court issued the requested preliminary injunction with respect to the staff already employed.

The appellate court reversed, holding that the defendant's good-faith reliance on a well-reasoned legal opinion trumped the plaintiff's claim of unfair business practice. However, the appellate court expressly allowed the case to precede to the Supreme Court for final clarification.

**Supreme Court ruling**

The Supreme Court upheld the appellate court's decision, but the court's reasoning will be a surprise to many.

The court acknowledged that enticing away employees by inducing them to breach their post-termination restrictive covenants had been qualified as unfair business practice by the court if the practice included a promise to indemnify employees against damage claims brought by their former employers; however, it stated that (following the 2007 amendment to the Unfair Competition Act) this rationale need to be reviewed in light of more recent legal literature.

As Austrian literature mainly aligns with the court's previous position, the court referred to the abundant German literature relating to comparable legal concepts in order to support its new position.

According to some German legal scholars, inducing employees to breach their contracts by indemnifying them against any legal consequences derives from a moralistic 'grandfathering' concerning the vested rights of decades past; thus, many legal scholars believe that this policy should have been eliminated by now, at least in the context of competition law. Further, it is difficult to draw a line between inducing a breach and taking advantage of a breach already committed by an employee without incitement.

The court went on to reiterate previous case law, which states that free competition includes demand for employees and that employers have no vested right to retain their workforce. As such, the court held that the hunt for the best talent does not prohibit potential employers from offering better terms to employees. In addition, the court held that, economically, there is no difference between a prospective employer offering a special sign-on bonus and agreeing to indemnify employees against damage claims pertaining to a breach of their non-compete clauses.

Consequently, the court held that the type of indemnification offered in the case at hand did not render the practice unfair as such. Only if certain additional circumstances occurred which amounted to a distortion of competition – in particular, if other aggressive or misleading business practices (the court did not specify further) were at play – could enticing employees away be considered unfair business practice.

In the case at hand, no aggressive or misleading practices were used.

**Comment**

The new precedent clarifies that enticing employees away from competing employers does not constitute an anti-competitive act as such – even if the new employer offers to indemnify its new hires against claims based on an alleged breach of their restrictive covenants.

The Supreme Court's decision has called into question which penalty clauses are useful when it comes to non-compete clauses. This question is not entirely new, as Austrian law states that employers that impose contractual penalties in employment contracts can request only the penalty, not specific performances or additional damages.

Given that the courts regularly mitigate contractual penalties and, as a result, penalties hardly exceed between 50% and 75% of employees' annual pay, they are not a strong deterrent and are therefore rarely useful.

Instead, employers should opt for specific performance clauses, without including contractual penalties. If the non-compete clause is reasonably worded and allows enforcement, neither the future employer nor the breaching employee can raise the defence that they were told otherwise by a reputable law firm and that they relied on the firm's advice.

*For further information on this topic please contact Jakob Widner at Graf & Pitkowitz Rechtsanwälte GmbH by telephone (+431 401 17 0) or email (widner@gpp.at). The Graf & Pitkowitz website can be accessed at www.gpp.at.*

**Endnotes**

(1) OGH 17.9.2014, 4 Ob 125/14g.

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