Collana Ravenna Capitale

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From International Treaties to the Binding Nature of Contract. A Historical and Comparative Study

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Post-Contractual non-competition clauses in German Labour Law – an example for today's law formed in practice

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1. Introduction

A detailed description of obligations is typical for the negotiation practice drawn up by jurists throughout the world. In large areas of Roman law, for example, the negotiation practice has played a key role in the creation of legislation.[1]

The oldest preserved Latin scripture, "*De agri cultura*", written around 150 BC by *Marcus Porcius Cato*[2] the Elder, shows that the discipline of „contracting" was born in the concreteness of an economic relationship and does not arrive at a conceptualisation.

Cato's famous *leges venditionis* are contained in the chapters 146-150 of "*De agri cultura*". Most of them are very detailed and give rise not only to primary obligations, but also to secondary obligations listed individually. Very often the obligations set out are guaranteed by oaths and normally the consequences of any breach are indicated so as to avoid any possible litigation.

Cato's leges are law formed in practice: the jurist knows all the necessary technical operations so as to be able to foresee possible errors or malicious behaviour.

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[1] G. Bassanelli Sommariva, *Due parole di introduzione: i formulari Catoniani quali documenti della prassi e dell'attività cautelare dei veteres*, in Ravenna Capitale Localizzazioni e tracce di atti negoziali (a cura di G. Bassanelli Sommariva), Santarcangelo di Romagna, 2020, 1 ff.

[2] Also known as the censor. M. Bretone, *Storia del diritto romano*, Roma, 2008[12], 172) calls him – along with Sextus Aelius and Manilius – "inventore di formule".

Just like the very well-known ideal of *Celsus* after which law is art and the jurist is a craftsman.[3]

Of course, it would be anachronistic to compare *Cato's leges*, which are born in a special economic and social context, with today's cautelar jurisprudence. The picture is much more complex than it seems at first sight, so we have to be very cautious with trying to find apparent similarities or parallels in these sources of juridical practice.

Nevertheless, in today's German law, contractual constructions can be found, in which the individual obligations of the parties are worked out in detail, with the same purpose: to prevent litigation. This contribution will examine some specific clauses of German Labor Law in practice and try to put them into a comparative context.

2. Legal Framework

In current German Labor Law, there is no one Labor Law Code, but there are many different legal and other regulations, as well as a large volume of court decisions, which the practitioner of German Labor Law must know and observe very well. Many areas, e.g. the important law on strikes, are not at all, or at least insufficiently, codified.[4]

This contribution focuses on the employment contract in case, which is within the legal framework the most important source of rights and obligations of the employee and the employer. But before we can take a closer look at the employment contract or more precisely at a specific clause of it, we need to understand the field of tension between the principle of private autonomy and the structural imbalance of power in German Labour Law.

3. Private autonomy and structural (im)balance of power in German Labour Law

The principle of private autonomy ("Privatautonomie") is a key doctrinal foundation of German civil law.[5] Unless the law provides otherwise, there is freedom of contract in working life, which means in particular freedom of contract content.

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[3] Dig. 1.1.1, Ulp. 1 *inst.*

[4] M. Lorenz, R. Falder, *Das deutsche und chinesische Arbeitsrecht - The German and Chinese Labour Law*, Wiesbaden, 2016, 104.

[5] According to Ch. Schaertl, *"Pacta sunt servanda – Basic principles of a Modern Contract Law"*, (in this volume) 18, the authors of the German Civil Code (BGB) voted for the Romanist understanding of private autonomy and freedom of contract and thus decidedly for a model of private law committed to Kant's ideal of freedom.

A diametrically opposed "principle"[6] of the German law is the protection of the "weaker party", which is expressed in particular in various employee protection laws (for example, the working time act, the labor protection act, the minimum wage act, etc.). We can therefore say that German Labor Law is to a large extent "social law"[7] (even if not "Social Law" in the strict sense)[8]. The largely employee-friendly case law further underscores this idea.

The German Labour Law creates a balance between the (supposedly) stronger bargaining position of the employer and the protection of employees' rights. The aim is therefore not to provide employers and employees with equal rights, but to elevate the employee to a near equal level of rights as the 'more powerful' employer.[9]

This leads to the assumption that the principle of contractual freedom only applies to a limited extent in German Labour Law. One of the reasons, for example, is that legal certainty[10] is required in favor of the employee and that the law of general terms and conditions does not provide the possibility to reduce an invalid provision to its legally permitted core ("Verbot der geltungserhaltenden Reduktion"). Therefore, an invalid contract clause will be eliminated entirely and the basic legal principles apply often with significant disadvantages for the employer[11].

In view of the special need for protection of the economically and personally dependent employee,[12] which is in a structurally inferior position,[13] the aforementioned basic freedom of contract ("Privatautonomie") is therefore subject to numerous limitations in German Labor Law. It is nowadays strongly limited through

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[6] We find this principle, for example, in consumer protection law or in tenant protection law, but also in the protection of minors.

[7] As mentioned before (see note 6) the German Private Law also contains a large number of provisions that are committed to social justice and security.

[8] On the distinction between German Private and Social Law, see E. Eichenhofer, *Sozialrecht und Privatrecht – Komplexe und komplizierte Wechselbeziehungen: Gedächtnisschrift für M. Heinze* (A. Söllner *hrsg)*, München, 2005, 145.

[9] Lorenz, Falder, *Das deutsche und chinesische Arbeitsrecht* ..., 103.

[10] As we see in section 74 German Commercial Code a non-competition clause, for example, must be in writing and a document signed by the employer and containing the agreed provisions must be handed over to the employee.

[11] Of course, this does not apply to individual contracts, but to employment contracts unilaterally drawn up by the employer.

[12] Ph. S. Fischinger, *Arbeitsrecht, Heidelberg,* 2018, 4: The consequence is that the employer can often present the applicant with a choice of "eat or die" in terms of working conditions. Thus, however, there is a lack of – at least approximate – negotiation equilibrium as a fundamental prerequisite of contractual freedom, which is not exhausted in a formal approach, but is based on the principle of genuine private autonomy in the sense of a self-determined decision on the if and content of a contract.

[13] Europäischer Gerichtshof (EuGH), 5.10.2004 – C-397/01; Bundesverfassungsgericht (BVerfG), 26.06.1991 – 1 BvR 779/85.

courts which may challenge the validity of a contract or its specific clauses,[14] e.g. of a post-contractual non-competition clause.

4. Obligations of fidelity and care

In German Labour Law the employee has the obligation of loyalty and fidelity to the employer (so-called "Loyalitäts- und Treuepflicht") and the employer has the obligation of care (so called "Fürsorgepflicht") to the employee as secondary obligations (section 241 II BGB).

These secondary obligations are not regulated in detail by legal norms. When determining their scope, specific circumstances of the case regarding the relationship between employer and employee have to be taken into account.

Here again, a cautious comparison can be made with Roman Law: Roman jurisprudence, and also the imperial legislation, delivered in *Justinian's* compilation, had no interest in constructing a typical figure of a contract of work performed by a free person under the directives of the employer. Of course, it has to be taken into account, that, in the Roman experience, work is predominantly the work of subordinates and that such relationships are totally unrelated to the world of obligations and contracts.[15] There is, however, no evidence of precepts regulating the contract and the relationship.[16] Another main difference between Roman and German Law, however, is that that the *fides* between the former *dominus* and the *libertus* arose from a potestative relationship.[17]

5. Post-Employment non-competition

a) General previous notes

During the employment relationship, the non-competition obligation for the employee arises from the previously mentioned obligation of loyalty as a secondary obligation (section 241 II BGB).[18]

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[14] Lorenz, Falder, *Das deutsche und chinesische Arbeitsrecht* ..., 103.

[15] L. Spagnuolo Vigorita, *Subordinazione e diritto del lavoro. Problemi storico-critici*, Neaples, 1967. But it is also Cato's "De agri cultura" which testifys the use of a *locatio conductio* to acquire work from the free to supplement the servile work, if necessary.

[16] V. Crescenzi, *"Per una semantica del lavoro giuridicamente rilevante in Isidoro da Siviglia, nella Lex Romana Visigothorum, nell'Edictum Theoderici, e nella Lex Visigothorum"*, in *Ravenna Capitale. Uno sguardo ad Occidente. Romani e Goti – Isidoro di Siviglia* (a cura di G. Bassanelli Sommariva, S. Tarozzi), Santarcangelo di Romagna, 2012, 217 ff.

[17] On personal dependency relationships in the Etymologiae of Isidore of Seville and from other sources of the Iberian provinces in the 5th-7th centuries see Crescenzi, *"Per una semantica del lavoro"* ..., 217 ff.

[18] It is important to strictly distinguish between pure secondary activity and competitive activity.

After termination of the employment relationship, the non-competition obligation does not continue to apply automatically (*post contractum*), but must be expressly agreed upon.[19] If the employer wants to effectively prevent the former employee from working as a competitor, a corresponding agreement for the period after termination of the employment relationship is required. This is possible in principle under section 6 II and section 110 of the German Trade Regulation (Gewerbeordnung).

For the protection of the employee, however, the indispensable (see section 75d German Commercial Code) provisions according to sections 74-75 f of the German Commercial Code apply accordingly, which contain specifications and restrictions for the post-contractual non-competition clause.[20]

This is due to the fact, that the basic rights of the employee weigh very high: After termination of an employment relationship, the employee is in principle free to compete with the former employer. This interest of the employee is protected by Article 12 of the German Constitution (GG).[21] In order to do justice to these interests of the employee, the provisions may not be deviated from to the disadvantage of the employee (section 75d German Commercial Code).[22]

Section 75d German Commercial Code sounds:

The principal ***may not invoke an agreement which deviates from the regulations of sections 74 to 75c to the detriment of the agent****. This shall also apply to agreements the purpose of which is to circumvent the statutory provisions on the minimum amount of compensation by offsetting or in any other way.*[23]

At this point, it is important to read how the above-mentioned regulations of the German Commercial Code sound like.

Section 74 German Commercial Code sounds:

*(1) An agreement between the principal and the assistant which restricts the assistant in his commercial activity for the period after termination of the employment relationship (****non-competition clause****) must be* ***in writing*** *and a* ***document signed by the principal and containing the agreed provisions must be handed over to the assistant****.*

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[19] The prohibition is usually included in a unilaterally pre-formulated employment contract, and generally only made with highly qualified employees or sales representatives with a strong customer connection, see Lorenz, Falder, *Das deutsche und chinesische Arbeitsrecht* ..., 115.

[20] Fischinger, *Arbeitsrecht* ..., 217-218.

[21] Concept of freedom of occupation of the employee ("Berufsfreiheit").

[22] Section 110 of the German Trade Regulation contains the prohibition of competition for employers and employees and says that section 74 to 75f of the German Commercial Code shall apply *mutatis mutandis*.

[23] Highlighting only here.

(2) The non-competition clause shall ***only be binding if*** *the principal undertakes to* ***pay compensation*** *for the duration of the non-competition clause which for each year of the non-competition clause shall* ***amount to at least half of the contractual benefits last received by the assistant****.*[24]

Section 74a German Commercial Code sounds:

(1) The non-competition clause shall ***not be binding insofar as it does not serve to protect a legitimate business interest of the principal****. It shall also* ***be non-binding insofar as, taking into account the compensation granted, it contains an unreasonable impediment to the advancement of the assistant in terms of place, time or object.*** *The prohibition may* ***not be extended to a period of more than two years*** *from the termination of the employment relationship.*[25]

b) Legal requirements

After having seen the codified law with its specific requirements, we dedicate ourselves to the contractual law in practice.

If we have a closer look at clauses recognized by case law in the field of post-contractual competition, we notice that they – following the requirements of the above-mentioned law as written – regularly contain a

1) temporal dimension,
2) spatial dimension,
3) content dimension and a
4) compensation for leave ("Karenzentschädigung").[26]

Often they also contain a contractual penalty, in case the employee violates the non-competition clause.[27] It is generally agreed – although not yet decided by the highest court – that a post-contractual non-competition clause is not subject to a review of the content of the general terms and conditions (AGB-Kontrolle),[28] but

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[24] Highlighting only here.

[25] Highlighting only here.

[26] Here a distinction must be made between the mere non-binding nature (see section 74 I Commercial Code) of the non-competition clause and its nullity: If a compensation for non-competition is promised, but in an amount that is too low, it depends solely on the employee's will, whether he or she observes the non-competition clause or not (see Bundesarbeitsgericht, Urt. v. 15.01.2014 – 10 AZR 243/13). If there is no compensation at all, the non-competition clause is null and void. For the difference see S. Naber, *"Nachvertragliche Wettbewerbsverbote ohne Karenzentschädigung – Nicht mehr zu retten!"* in *Neue Zeitschrift für Arbeitsrecht* (*NZA*), 2017,1171.

[27] However, high demands are to be made on their drafting. See in this regard: *H*-P., Winterstein, *„Nachvertragliches Wettbewerbsverbot und Karenzentschädigung"* in *Neue Juristische Wochenschrift* (*NJW*), 1989, 1466.

[28] Other opinion: J. Koch, "*Das nachvertragliche Wettbewerbsverbot im einseitig vorformulierten Arbeitsvertrag"* in *Recht der Arbeitgeber* (*RdA*), 2006, 28-33.

is governed exclusively by the finely balanced regulatory mechanism of sections 74 German Commercial Code, differentiating between nullity and non-binding nature.[29]

c) Example of a post-contractual non-competition clause

For a better understanding, we have to take a closer look at a post-contractual non-competition clause from practice:

"For a period of twelve months after termination of the employment relationship, the employee is prohibited from competing with the employer. The post-contractual non-competition clause refers:

- Factually to the area of … [content of the work activity] and there to all occu*pational groups in which the employer is currently active [...],*

- Spatially to the territory of ... [e.g. the Federal Republic of Germany; a radius of x kilometers etc.]

The employer undertakes to pay the employee compensation for the duration of the non-competition clause, which shall amount to half of the contractual benefits last received by the employee for each year of the non-competition clause. The employer must take into account any other acquisition in accordance with the statutory provision in Section 74 c of the German Commercial Code. If the employee violates the non-competition clause, he shall be obliged to pay the employer a contractual penalty in the amount of x % of gross monthly remuneration."

6. Case law

a) Legitimate business interest

In the year 2014, the Munich Higher Regional Court[30] had to decide on the extent of the legitimate business interest of midwifery practice as the defendant and former employer. In that case clause 9 of the contract in dispute with the heading "Protection against competition" read:

"The midwife has neither an employment relationship nor an employee-like relationship with the midwifery practice. Labour law regulations do not apply. After termination of the contractual relationship – for whatever reason – the midwife is prohibited for a period of two years after the end of the contract, to open a

[29] See note 25.

[30] See Oberlandesgericht (OLG) München, Urt. v. 15.01.2014 - 20 U 3001/13. The first instance in this case was the Landshut District Court. The court partially upheld the plaintiff's action. For further details see Landgericht (LG) Landshut, Urt. v. 05.07.2013 – 44 O 92/13.

practice as a midwife within a radius of 25 km from the … (regional area) and her colleagues to open a practice as a midwife or to become a freelancer or partner in a new or existing midwife practice or similar. The midwife will also not work and cooperate with hospitals in the aforementioned regional area, unless the midwife's practice has given its consent. In the event of a breach of this competition protection clause, the midwife undertakes to pay a contractual penalty in the amount of 20,000 €."[31]

This clause prohibited the midwife plaintiff from providing services to all female patients within a radius of 25 km of any of the plaintiff's practice, and thus also corresponding cooperation with all doctors and hospitals in this area and thus also the provision of services to and cooperation with such persons, with whom the plaintiff hadn't had any contact yet.

According to the legal opinion of the court, such a far-reaching regulation, moreover, without any compensation, violates section 138 I of the German Civil Code (immoral legal transaction) in conjunction with Article 12 I of the German Constitution (freedom of profession).[32] The competition protection and contractual penalty clause in clause 9 of the contract were therefore invalid.

The court stated that a non-competition clause is only valid, if it does not exceed, in terms of place, time and subject-matter the beneficiary's interests worthy of protection and does not unduly limit the freedom of profession. Consequently, a balancing of interests must take place in each individual case.

b) Post-contractual non-competition and severability clause

In the year 2017, the German Federal Labor Court had to decide on the question of how a severability clause ("Salvatorische Klausel") in an employment contract affects an invalid post-contractual non-competition clause.[33]

The senate was of the opinion that a post-contractual non-competition clause, which – contrary to section 74 II of the German Commercial Code – does not

[31] The clause reads *verbatim*: "Der Hebamme ist nach Beendigung des Vertragsverhältnisses - egal aus welchen Gründen - für den Zeitraum von zwei Jahren nach Vertragsende untersagt, im Umkreis von 25 km um die Praxisstandorte […] Kolleginnen eine Praxis als Hebamme zu eröffnen oder sich als freie Mitarbeiterin bzw. Gesellschafterin einer neuen oder bestehenden Hebammenpraxis oder ähnliches niederzulassen. Auch Tätigkeiten und Zusammenarbeiten mit Krankenhäusern im vorgenannten regionalen Bereich wird die Hebamme unterlassen, soweit nicht eine Zustimmung der Hebammenpraxis vorliegt. Für den Fall der Zuwiderhandlung gegen diese Konkurrenzschutzklausel verpflichtet sich die Hebamme zur Zahlung einer Vertragsstrafe in Höhe von 20.000 €."

[32] Section 74 II of the Commercial Code did not apply to the present contractual relationship between the parties, even by analogy.

[33] Bundesarbeitsgericht (BAG), Urt. v. 22.03.2017 – Az.: 10 AZR 448/15.

contain any compensation for non-competition, is void by operation of law. A severability clause is not suitable for eliminating or curing this consequence. One of the legal reasons given was that the severability clause did not provide the before mentioned legal certainty required in favor of the employee:[34]

The employee shall not be prejudiced in his search for a new job by being left in the dark as to whether or not he is subject to an effective restriction of competition [...],

Therefore, the obligation to pay the waiting compensation ***must be the content of the written competition agreement and must be formulated in such an unambiguous and clear manner that, from the employee's point of view, no reasonable doubt remains as to his entitlement to compensation***.[35]

In combination with the severability clause, the required legal certainty for the employee does not exist in this case. As the German Federal Labor Court states, it is furthermore unclear by which regulation a severability clause is supposed to replace the lack of compensation. It would even lead to an absurd result to apply the law to these cases: If we take the legal minimum amount of compensation (in accordance with section 74 II Commercial Code) as a substitute regulation, an employee, with whom no compensation at all has been agreed, would be in a better position than someone, who has only been promised an insufficient compensation.[36]

7. Conclusion

The German Labour Law organises the exchange of labour performance for remuneration, which is of the greatest importance in our society, that is geared towards securing a livelihood through dependent employment.

Secondary obligations of fidelity in dependent employment relationships are not regulated in detail by legal norms. Even if there is a legal framework for clauses on the post-contractual prohibition of competition, the parties' obligations in detail must be regulated individually.

The heart of the post-contractual non-competition clauses is certainly the compensation for non-competition.

The most detailed formulated clauses testify to the fact that the parties try to avoid going to court as much as possible. Here the legal practice shows itself to be

[34] Bundesarbeitsgericht (BAG), Urt. v. 22.03.2017 – Az.: 10 AZR 448/15, marginal no. 34.
[35] Highlighting only here.
[36] Compare Naber, *"Nachvertragliche Wettbewerbsverbote"* ..., 1172.

very innovative. It is also very important to diligently and continuously create and update the contract clauses. Practitioners of German Labour Law know very well that special care must be taken when drafting post-contractual non-competition agreements. Severability clauses are not a sufficient basis for the rescue of post-contractual non-competition clauses.

As we have seen, the German Federal Labour Court protects the employee when it presupposes that a post-contractual non-competition clause has to be formulated in such an unambiguous and clear manner that, from the employee's point of view, no reasonable doubt remains.

In this respect, we can summerise the said with a quote according to *Mario Bretone*:

"The law, any law, is superfluous when the jurisprudence is able by itself to suggest the criteria for solving a practical problem; the law is necessary on the other hand, when the practical problem is not otherwise solvable."[37]

[37] Bretone, *Storia* ..., 182.