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THE GOOD, THE BAD AND THE AWKWARD

HOW TO SUCCESSFULLY USE COMPROMISE AGREEMENTS & SEVERANCE TERMS IN GERMANY

By Jan Tibor Lelley & Frederike Meermann



A COMPROMISE AGREEMENT HAS THE ADVANTAGE OF TERMINATING THE EMPLOYMENT CONTRACT AT SHORT NOTICE AND, FROM THE MANAGEMENT'S POINT OF VIEW, WITH A MINIMAL RISK.



Anyone who has concluded an employment contract can also cancel it by mutual agreement. These agreements are known as compromise agreements, severance terms or termination agreements. The term does not really matter as long as one looks carefully at the circumstances and legal requirements such agreements entail.

Always a win-win?

A compromise agreement is a contractual agreement between an employer and an employee by which the employment relationship is terminated by mutual agreement at a certain point in time. A compromise agreement has the advantage of terminating the employment contract at short notice and, from the management's point of view, with a minimal risk. It can be differentiated from the fixed-term employment contract in that the termination of the employment relationship is not part of the employment contract but is agreed upon after its conclusion. When an employment contract is terminated by agreement, the employee is therefore not in the same pressure situation as when concluding a fixed-term employment contract, where the main aim is to secure the position.

The compromise agreement has advantages for the employer:

- The employment relationship may be terminated without complying with statutory, collectively agreed, or individual contractual notice periods.
- Both general and special protection against termination (like the German Unfair Dismissal Protection Act) do not apply.

- Any works council does not need to be involved.

But the employee also has advantages from a compromise agreement:

- The notice periods can be shortened, which could conflict with a possible immediate start of work with another employer.
- In the event of serious misconduct by the employee, which could result in dismissal without notice, "unsuspicious" termination dates for the employment relationship can be agreed by means of a compromise agreement.
- A compromise agreement can provide an opportunity for the employee to explore new career paths or seek better job prospects. It can be a chance for personal and professional growth, as they may find a more fulfilling role or pursue further education or training.
- Sometimes, an employment relationship becomes strained, leading to a negative work environment. In such cases, parting ways by using a compromise agreement can relieve stress and create the option for a fresh start for both parties involved.

However, there are also some disadvantages to be considered when concluding a compromise agreement:

- Termination of an employment agreement can have a significant financial impact on both the employee and the employer. Employees may face a sudden loss of income, which can be especially challenging if they have financial obligations or dependents. Employers, on the other hand, may incur costs associated with severance packages or legal fees.

- Losing a job can have a profound impact on an individual's emotional and psychological well-being. It may lead to feelings of uncertainty, low self-esteem, or even depression. Similarly, employers may experience guilt or a sense of failure when ending an employee's contract.
- Terminating an employment agreement can disrupt the workflow and dynamics within the organisation. It may require redistributing tasks, hiring and training new employees, or adjusting team structures. This can result in temporary inefficiencies and additional workload for remaining staff.
- Improperly handled compromise agreements can lead to legal consequences for both employers and employees. Disputes may arise regarding severance packages, non-compete agreements, or even wrongful termination claims in court. Legal proceedings can be time-consuming, costly, and further strain relationships.

Know the ropes: Formal requirements for a compromise agreement

German employment law stipulates requirements for the conclusion of a compromise agreement. For instance, the agreement must be in writing. The written form requirement also extends to changes made subsequently. A tacit agreement is generally not possible. The termination agreement must be signed by both parties on one document. This means wet-ink signature. Compromise agreements which do not comply with this statutory formal requirement are invalid. In accordance with the principles of good faith, compromise agreements agreed upon without considering the formal requirements may, in exceptional cases, be enforceable – if their invalidity is due to the lack of written form and would not only be harsh for one of the parties but would also be merely intolerable. This is, for example, in the event of a threat to the existence of the company, fraudulent intent or serious breaches of fiduciary duty.

A compromise agreement, like any other agreement, is concluded by offer and acceptance. If the agreement contains several pages, they must be combined (e.g. staple the pages together).

Content requirements

The condition of a compromise agreement, formulated by the employer, must be clear and unambiguous and must not be surprising according to the appearance of the contract. Whether an agreement is a compromise agreement or a fixed-term continuation of the employment relationship depends on its content. A right to withdraw may be agreed in the compromise agreement. Without that, an employee cannot withdraw from such an agreement after he has signed it. A compromise agreement can be combined with a broader settlement agreement. Such an agreement also settles outstanding claims upon termination of the employment relationship and resolves disputed claims, which may facilitate putting to rest an already terminated employment relationship.

Duties of disclosure

There are also duties of disclosure regarding compromise agreements. When considering the extent of the duty to inform, the employee's recognisable need for information and the employer's possibilities to provide advice must be weighed up in each individual case. It can be assumed that the employee will consider the consequences of a termination agreement before concluding it and must inform himself about the legal consequences, if necessary. Information regarding a potential impact on the employee's social security status can be expected if the employer is aware that the employee requires further information and that he himself cannot obtain the information without any difficulty. But, after all, if the employer does not inform the employee about the potential consequences, the compromise agreement remains enforceable.

Limits of compromise agreements

Compromise agreements do not eliminate the legal consequences of a Transfer of an Undertaking (TUPE). If the employer induces employees to conclude compromise agreements in order to give the acquirer of a business the opportunity to conclude employment contracts with less favourable terms or to be able to choose the employees, the agreements are invalid. Generally, compromise agreements are also invalid if a new employment relationship with the business acquirer is agreed upon at the same time, thus the agreement does only serve the purpose of eliminating a continued employment relationship although the job is retained.

In conclusion, while using compromise agreements can bring positive outcomes such as mutual consent and opportunities for growth, it also carries some negative aspects, including financial impact, emotional effects, potential disruption to the workforce, and legal risks. It is crucial for both parties to approach the situation with sensitivity, fairness, and open communication to minimise negative consequences and foster a smoother transition. However, companies are well advised to conclude to aim for a compromise agreement rather than just terminating the employee's contract. There is always a risk that the employee would take legal action to challenge the termination and one sees each other in the labour court.



Dr Jan Tibor Lelley LL.M. is a partner with BUSE and he is a member of the firm's Practice Group Employment. Jan works exclusively on labour and employment law cases. With more than 20 years of professional experience, he advises employers and HR executives on the full range of HR related legal issues and key areas. Clients regularly trust Jan with their most challenging, complex and high-risk matters and negotiations with works councils, unions and representation in the courts.

Frederike Meermann is a legal trainee at BUSE's Essen office. She went to law school in Passau and Hamburg and passed her first state exam in 2022.



For more information please contact:
+49 6998972350 | lalley@buse.de