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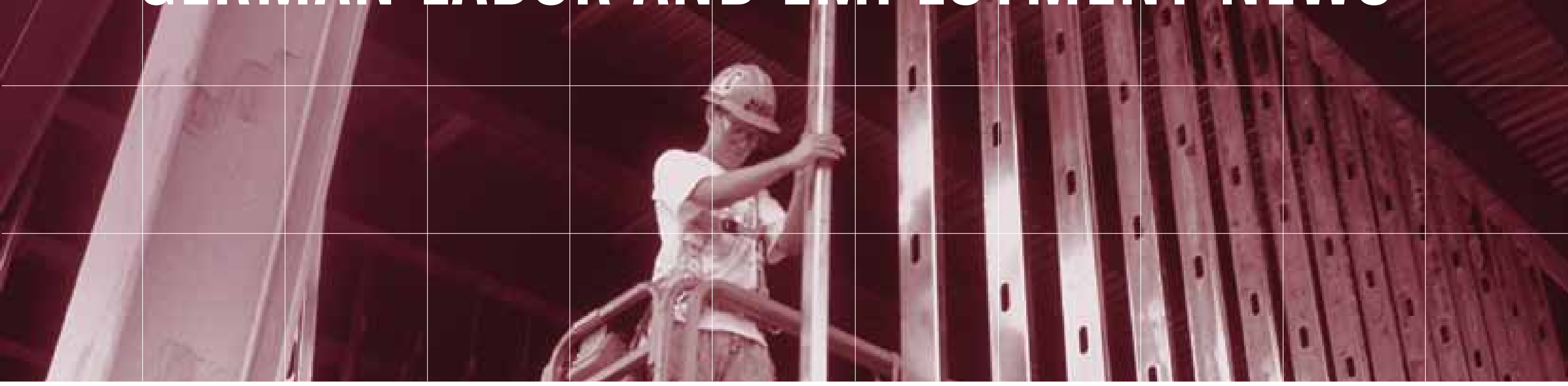

SEX DISCRIMINATION WITH RESPECT TO JOB PROMOTION: THE EMPLOYER'S FINANCIAL CONSEQUENCES

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In Germany, just as in many other countries, women are often subject to indirect discrimination in the workplace. A German court of appeals has now accepted that a company's hiring statistics can be an indication that an employer discriminated against a woman on the basis of gender.

The plaintiff, a female, had graduated with an MBA. She had initially been hired to work in the human resources department of a company that had more than 1,100 employees. Although 69 percent of the company's employees were women, the 27 highest managerial positions were filled by men. When the position of HR director became available and the company did not consider promoting the plaintiff, she sued under Germany's Equal Treatment Act, which prohibits discrimination in the workplace. The court ruled in her favor.

STATISTICAL EVIDENCE

Under the General Equal Treatment Act, a plaintiff-employee must be able to demonstrate only that there was an "indication" of discrimination in the workplace. If the plaintiff is able to satisfy this threshold, the burden of proof is then transferred

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When an individual alleges discrimination in connection with a promotion, the General Equal Treatment Act does not permit the plaintiff to make a claim for specific performance (*i.e.*, to be promoted); instead, only monetary damages may be awarded.

to the employer-defendant, who must be able to prove that there was in fact *no* discrimination.

The court of appeals allowed the plaintiff to introduce company statistics on male/female ratios in the workplace to demonstrate that she was the victim of sex discrimination; this statistical evidence was sufficient to demonstrate an "indication" of discrimination. The court took into consideration that, even though women comprised more than two-thirds of the company's staff, men held all 27 senior-level positions. This, plus the fact that the female plaintiff had been passed over for a promotion that was eventually given to a man, was an *indication* of discrimination. In addition, the court of appeals considered historical data involving the company, specifically, that in the last 30 years of the company's history, only one woman had held a senior-level position.

THE EMPLOYER'S COUNTERARGUMENT

The defendant company was unable to refute successfully the plaintiff's claim of discrimination. Adding to the company's difficulty in making its case was that it was permitted to present only the information concerning its hiring decision that had been made known to the candidates during the job-application process. Since the company had failed to note that a university-level degree was a prerequisite for the job (the company had not prepared a job description or any other written material), it was not permitted to present this significant fact to the court when it presented its case.

COMPENSATION FOR FINANCIAL LOSSES

When an individual alleges discrimination in connection with a promotion, the General Equal Treatment Act does not permit the plaintiff to make a claim for specific performance (*i.e.*, to be promoted); instead, only monetary damages may be awarded. The court of appeals' decision was unique, however, in that it ruled that the plaintiff was entitled to monetary damages for the duration of the employment relationship. The employer was required to pay the difference between what the plaintiff actually earned and what she would have earned had she been promoted.

COMPENSATION FOR NONFINANCIAL LOSSES

The court of appeals also established that the sex discrimination constituted a violation of the individual's right to be treated with integrity, meaning monetary damages were warranted for this violation as well. However, the court awarded the plaintiff only €4,000 for the violation of this right; it held that a higher amount was not justified, as the court had already awarded the plaintiff damages for the actual financial losses she had suffered.

Moreover, the court concluded that the employer's derogatory and intimidating treatment of the plaintiff on the day she informed the employer that she believed her rights had been violated under the General Equal Treatment Act also violated the plaintiff's right to be treated with integrity. As a result of this violation, the plaintiff was awarded an additional €16,000.

However, because there was no indication of any violence or threats of violence against the plaintiff, her health was not impaired as a result of the discrimination, and no real insults had been levied against her, the court rejected the plaintiff's claim for an additional €70,000 in damages; this had been reduced from the €390,000 initially sought at the trial-court level.

This court's decision to keep damages at a reasonable level is in line with decisions from other labor courts. For example, a discrimination case had been filed against the R+V Versicherung insurance company in Wiesbaden, Germany. In its decision of December 18, 2008, the court agreed that the female plaintiff suffered discrimination when she returned from maternity leave to find herself demoted to a lower-paying position and her former job given to a male. Though the plaintiff sought €43,000 in damages, the trial court awarded her only €10,818 (equal to three months of her salary), rejecting in its entirety the plaintiff's additional claim of €433,000 as compensatory damages.

PRACTICAL TIPS

It remains to be seen whether the Federal Labor Court will uphold the court of appeals' decision referenced above. Regardless, employers should make sure to keep their decisions regarding promotions transparent; *e.g.*, make sure a written job description has been prepared. Otherwise, refuting an employee's "indication" of discrimination may be nearly impossible, as the employer will be limited in the evidence it may present.

Germany's Federal Vacation Act calls for a minimum of 24 days of vacation per year and sets forth that if an employee is ill during his vacation, the days on which he was ill will not count as vacation.

ACCRUED VACATION DAYS FOR EMPLOYEES ON LONG-TERM DISABILITY: A POTENTIAL FINANCIAL BURDEN FOR EMPLOYERS

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Gerhard Schulz-Hoff had been hired by the German Federal Pension Federation in 1995. Severe back problems during his employment caused him to undergo more than a dozen operations. Finally, in September 2004, because of his back problems, he was put on long-term disability until his eventual retirement in September 2005.

As soon as he went into retirement, he sought financial compensation from his employer for the vacation days that had accrued during his period of disability. Mr. Schulz-Hoff

based his argument on an extended interpretation of Germany's Federal Vacation Act, which calls for a minimum of 24 days of vacation per year and sets forth that if an employee is ill during his vacation, the days on which he was ill will not count as vacation. Because he had been ill for more than a year, he had not used any vacation days during that entire period.

Not surprisingly, his employer was of the opinion that Mr. Schulz-Hoff had forgone these vacation days because, as is also set forth in the Federal Vacation Act, an employee must generally take his vacation in the calendar year in which the vacation accrued. If the employee fails to take his vacation during that calendar year, he has until March 31 of the following year to use up his vacation days. End result: If an employee fails to take his vacation days by the end of March of the year after they accrued, they are lost; the employee can no longer take those vacation days, nor does he have a claim to compensation for having failed to take the vacation days.

GERMAN LAW VS. EUROPEAN LAW

Mr. Schulz-Hoff subsequently sued his former employer, seeking compensation for the lost vacation days during the years 2004 and 2005. This action was eventually brought before the European Court of Justice ("ECJ") because it raised a couple of fundamental issues:

1) In failing to require at least four weeks of vacation for *all* employees (including those who, like Mr. Schulz-Hoff, are on long-term disability), does Germany's Federal Vacation Act violate EU law?

2) In failing to require financial compensation to be paid to employees who were not able to take their vacation days due to incapacitation, does Germany's Federal Vacation Act violate EU law?

The European Court of Justice answered yes to each of the above questions. Germany's Federal Vacation Act does indeed violate EU law—in particular, Article 7 of EU Directive

Ergo, if an employee is not working, he does not need a vacation to relax or to become rejuvenated. This, unfortunately, contradicts Directive 2003/88, which states that *every* worker is entitled to a paid annual leave—no mention is made as to the specific purpose of the leave.

2003/88, which states that each EU member state must "ensure that *every* worker is entitled to paid annual leave of at least four weeks" (emphasis added); no exception is made for employees who are on long-term disability or otherwise prevented from taking their vacation.

Some commentators have argued, quite persuasively, that the ECJ's finding is erroneous because the purpose of a vacation is to allow an employee to recuperate from work and to become rejuvenated. In particular, Germany's Federal Vacation Act specifically states that "all workers have a claim to paid vacation for *relaxation* every calendar year" (emphasis added). Ergo, if an employee is not working, he does not need a vacation to relax or to become rejuvenated. This, unfortunately, contradicts Directive 2003/88, which, as mentioned above, states that *every* worker is entitled to a paid annual leave—no mention is made as to the specific purpose of the leave.

CONSEQUENCES OF THE ECJ DECISION

Ironically, though the ECJ's decision may initially seem to be a sort of financial windfall for employees on long-term disability, the practical consequence may well be that employers will decide to terminate those employees, for the simple reason that the employees' vacation accruals will continue to add up for the duration of the disability. Whether this will actually happen depends largely on whether the appeal filed by the employer is successful.

Up to now, employers typically would forgo terminating employees on long-term disability because these employees were not a cost factor; after six weeks of sick leave, the employee no longer earns his salary, but instead receives disability benefits from his health insurance and thereafter (depending on the circumstances) either unemployment benefits or a pension.

Employers should note that they can terminate an employee on long-term disability only if they can demonstrate that the employee is no longer able to perform his work due to the disability. This raises the question, however, of how long the prognosis for the continued disability must be before the employee is deemed unable to return to work. As can be imagined, this depends on the situation at hand, but the general rule of thumb is that if an employee is not able to return to work within two years (usually according to a doctor's certificate), the employer will have met his burden of proof.

From an M&A perspective, buyers are well advised to pay more attention to whether and how many employees of the target company are on long-term disability. The more employees on long-term disability, the greater the potential financial burden for the buyer, as these employees may eventually make a claim for the accrued, but unused, vacation days.

COMPANY PENSIONS ARE SECURE (AT LEAST, FOR THE MOST PART)

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As many employers can attest, the current financial crisis requires them to pay greater attention to costs and expenditures than ever before. Saving on human resources costs was discussed in the previous edition of *German Labor and Employment News* (see "The Financial Crisis—Cost-Saving Measures Without Terminating Employees"). To the more well-known employee costs of wages, salaries, and

From a practical perspective, it is unlikely that a court will rule that an employer may unilaterally amend a pension plan.

bonuses may now be added company pensions. It should be no surprise that German labor courts are now confronted with the issue of whether, and to what extent, a company may reduce company pension benefits.

An employer's decision to allow an employee to participate in a company pension plan constitutes a contractual obligation between the two parties, either individually with the employee or collectively with the works council or union. Though discontinuing such a pension plan would permit the employer to reduce its costs, such a discontinuation can be effective only with respect to newly hired employees. This, however, raises the question of how long the employer must observe its contractual obligation vis-à-vis current employees to keep a pension plan in place. Theoretically, the employer should be required to keep the pension plan in place not only for as long as the employee lives, but also for the life of that employee's heirs. Because this would be an undue burden on employers, however, past Federal Labor Court decisions have confirmed that under certain circumstances, an employer may amend pension plans during the "life" of the plan.

PENSION OBLIGATIONS VIS-À-VIS AN INDIVIDUAL EMPLOYEE

If an employer agrees to the terms of a pension plan directly with the employee (*e.g.*, as part of a written employment agreement), the employer may amend the pension plan's terms only by letting the employee know that it wishes to amend the pension plan and that if the employee does not accept the proposed amendment, the employer has no choice but to terminate the employee. (This is based on the principle in German employment law that an employer may not unilaterally change the terms of an employee's employment agreement.) The employee then has three options in response to the employer's notification: (i) to accept the proposed amendment; (ii) to reject the proposed amendment with the understanding that the employee will lose his job; or (iii) to accept the proposed amendment with the understanding that a labor court is to review whether the employer may in fact introduce that amendment. If the employee chooses the third option, the employee and the employer will be bound by the court's decision. From a practical perspective, it is unlikely that a court will rule that an employer may unilaterally amend a pension plan.

PENSION OBLIGATIONS VIS-À-VIS THE INDIVIDUAL EMPLOYEE WITH A COLLECTIVE COMPONENT

If an employer agrees to a pension plan by way of an agreement with the works council or by way of a "company practice" (*i.e.*, the plan was agreed to implicitly because it had become standard practice over time, with the result that the employees now have a *legal claim* to it), then an individual employee may still enforce it, even though it has a collective component to it. As with the above scenario, from a practical perspective, an employer will have a tough time successfully amending the terms of a pension plan unilaterally.

One method of amending a pension plan is by concluding a superseding works agreement. Ignoring for the moment the issue of whether an employer may introduce such an agreement, it must be admitted that this will not allow the employer to save on costs, since German pension law subscribes to the principle that even though specific costs may be redistributed among the employees, the employer's *aggregate* costs must remain unchanged. As a result, the employee's aggregate benefits would not be decreased.

COLLECTIVE PENSION OBLIGATIONS

In today's world, a large percentage of companies conclude a company pension plan by way of a written agreement with the works council (the so-called works

Case law has set forth, however, that works agreements have a salary component to them. As a result, an employer does not have free reign to terminate a works agreement at any time; instead, the termination must be reasonable and protect the employees' concept of trust vis-à-vis the employer.

agreement); such an agreement constitutes a "collective" obligation on the part of the employee. Works agreements may be terminated at any time without cause. Case law has set forth, however, that works agreements have a salary component to them. As a result, an employer does not have free reign to terminate a works agreement at any time; instead, the termination must be reasonable and protect the employees' concept of trust vis-à-vis the employer. An employer may amend a pension plan only under certain circumstances:

1) Accrued Vested Pensions

The first type of pension involves rights that have already vested. It is nearly impossible for an employer to amend these pension rights because the employee has already met his end of the bargain (*i.e.*, worked for the employer until the pension became vested). The only way for the employer to satisfy his end of the bargain is by making the payments as set forth under the pension plan.

2) Employees' Partially Vested Pension Rights

These types of pension benefits are tied directly to the employee's most recently earned salary. Amending the basis for the calculations could cause the employee's salary at the time of the amendment to actually constitute the "most recently earned salary." An even more significant impact would result if the employee was deemed to have left the company as of the date the amendment to the pension became effective. In such an event, any years of service subsequent to the amendment would not be counted. German courts, however, permit employers to introduce such an amendment only if there is just cause: *e.g.*, if the company would otherwise be in financial straits. To put it succinctly, a company may amend such a pension plan only if it is otherwise unable to meet its financial pension obligations or if meeting those obligations would jeopardize the company's viability.

3) Unvested Pension Rights

Future increases in pension rights that are not to be maintained if the employee leaves his employer on a specific day may be amended in the event of corporate distress. This includes increases in benefits, such as annual pension increases, that depend on years of service. The employer may not arbitrarily decrease pension benefits; instead, any such decrease must be in proportion to the reason for the decrease.

CONCLUSION

Saving money by amending company pensions, though possible, is an option only if the pension benefits are the subject of a works agreement. Additionally, amendments may lead only to future cost savings. For an employer to try to save costs on vested pension rights—*i.e.*, to remove them from the balance sheet—is essentially impossible.

THE DEVELOPMENT OF THE PRINCIPLE OF EQUAL TREATMENT

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The enactment of the German General Equal Treatment Act in August 2006 left many wondering what ever happened to Germany's principle of equal treatment. After all, this had been developed by the courts and had been in effect for decades. The short answer: It may have changed a little, but it is still an important legal principle in its own right.

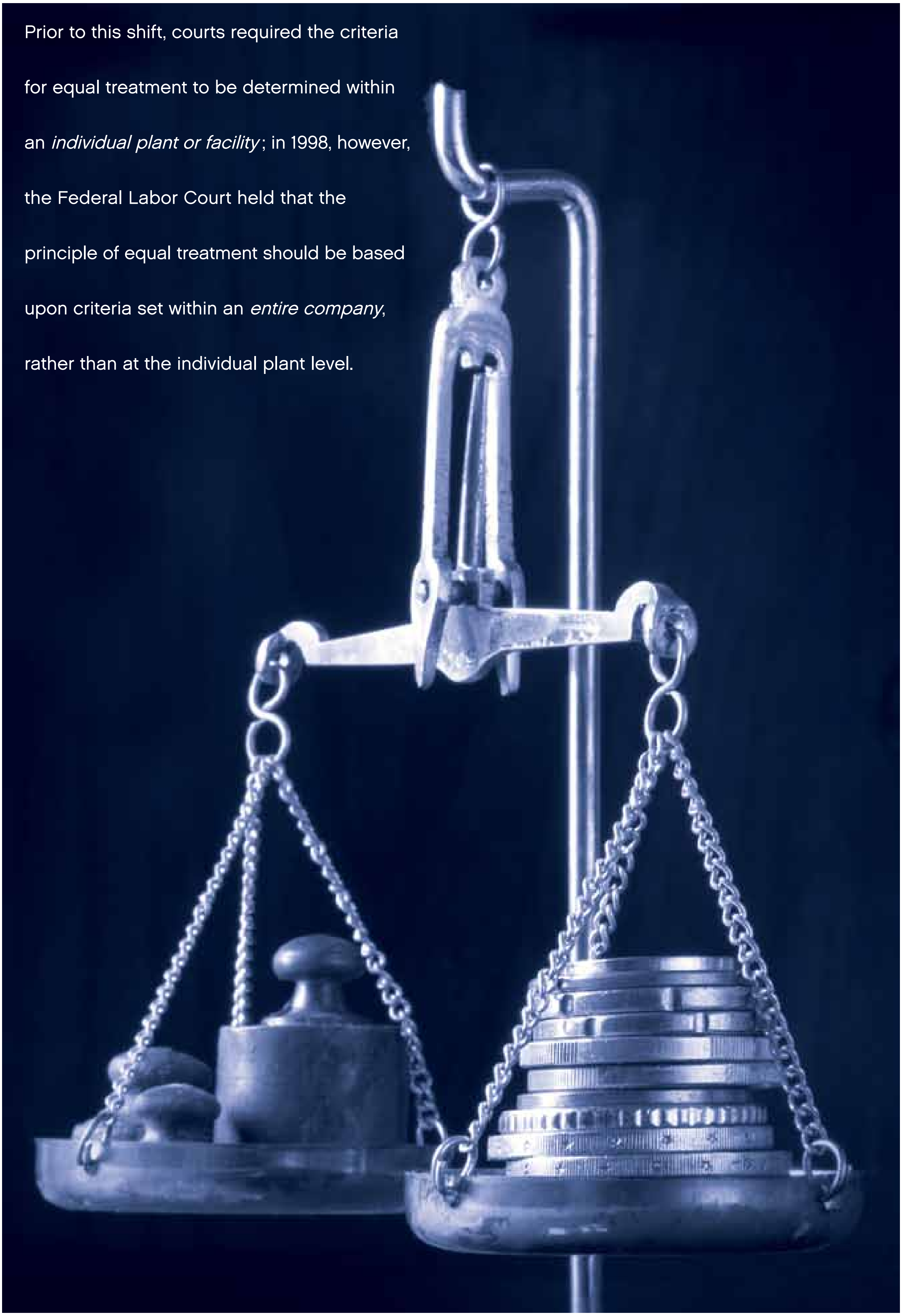
THE PRINCIPLE OF EQUAL TREATMENT VS. THE GENERAL EQUAL TREATMENT ACT

The principle of equal treatment is based primarily on the equal treatment requirement as set forth in Germany's Constitution. This principle requires substantially equivalent situations to be handled in the same way; only substantially different situations may be treated differently.

In contrast, the General Equal Treatment Act, which is based on European Union law, focuses on discrimination based on specific criteria, such as age or ethnic origin. However, when the question arises whether it is proper to grant more benefits to a 35-year-old clerk of German origin than to his colleague next door—another 35-year-old German clerk who is performing the same job—the courts refer to the principle of equal treatment.

If an employee alleges unequal treatment, the risk to the employer is that the disadvantaged employee's benefits will increase (as opposed to the favored employee's benefits

Prior to this shift, courts required the criteria for equal treatment to be determined within an *individual plant or facility*; in 1998, however, the Federal Labor Court held that the principle of equal treatment should be based upon criteria set within an *entire company*, rather than at the individual plant level.



decreasing). However, case law favors employers in this regard, because if the group of favored employees is relatively small—less than 5 percent of the employees, according to one decision—the other employees will not be in a position to claim unequal treatment.

THE DEVELOPMENT OF THE EQUAL TREATMENT PRINCIPLE

German case law experienced a major shift with respect to the principle of equal treatment about 10 years ago. Prior to this shift, courts required the criteria for equal treatment to be determined within an *individual plant or facility*; in 1998, however, the Federal Labor Court held that the principle of equal treatment should be based upon criteria set within an *entire company*, rather than at the individual plant level. This has now been the case since 1998.

As a consequence, not only are individuals now compared to one another, but the workforce of a plant must also be compared to that of another plant. For example, the courts state that unequal treatment of the workforces at two different plants may be permitted if the plants belong to different industrial sectors, or even if the plants are experiencing different economic situations. Individual plants' different "histories" may also be grounds for unequal treatment. For example, if a business is acquired by way of an asset deal, the buyer is not necessarily required to grant the employees of the target plant the same benefits that had been granted to the employees who were not part of the acquisition.

The applicability of the principle of equal treatment to comparisons of the workforces of different plants was also implied when the Federal Labor Court ruled on whether granting certain benefits to employees of only one plant may be justified on the grounds that the plant's works council approved a works agreement on working time. This works agreement gave the employer greater flexibility on working-time issues than was the case at another plant, where the works council did not agree to such flexibility. The Federal Labor Court stated that the added flexibility in working time at one plant could justify the otherwise unequal treatment between the two plants.

In another case, an employer granted a voluntary salary increase at the company level, but with the proviso that only employees of financially successful company sites could benefit from the increase. The Federal Labor Court held that this was permissible because an employer is entitled to encourage competition among its sites and may take into account the profitability of each. Somewhat surprisingly, the court went so far as to permit the employer to determine which sites could benefit from the salary increase, as long as the employer did not act arbitrarily.

EQUAL TREATMENT WITHIN A PLANT

The Federal Labor Court is not as generous in those cases where individual employees, rather than plants, are to be compared. Within the context of company pensions, the court held that an employer can exempt certain individuals from a generally entitled group of employees as long as the pension plan sets forth the respective criteria to determine whether employees are eligible and as long as those criteria are sufficiently clear. In that particular case, the court held that the pension plan was too imprecise, as the criteria were not sufficiently specific; *e.g.*, it made references to "increased" production without setting forth specific criteria.

An employee must ensure that allegations of unequal treatment are not just general assertions. The Federal Labor Court has emphasized in the past that a conclusive assertion of a violation of the equal treatment principle cannot consist merely of statements that a compensation system is not transparent and is not applied in a uniform manner.

The principle of equal treatment prohibits not only the arbitrary disadvantaging of individual employees within a group, but also the inappropriate establishment of groups. More and more courts view the principle of equal treatment as a company issue rather than a plant issue. When considering the appropriateness of, and justification for, different treatment among entire plants, courts are relatively lax; even economic factors or the desire to encourage competition between plants may serve as a justification for unequal treatment. Regardless, an employer must always be able to apply the criteria for the unequal treatment clearly and in a transparent manner.

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