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# Directive 77/187: The EEC'S Attempt to Protect Employees upon the Sale or Transfer of Businesses

## I. INTRODUCTION

In February 1977, the Council of the European Communities adopted Directive 77/187.<sup>1</sup> The purpose of the directive is to safeguard the rights of employees of businesses that are sold or transferred. The directive seeks to protect employees in three ways. First, it provides for the automatic transfer of the former employer's obligations to the new employer.<sup>2</sup> Second, it prohibits the dismissal of employees solely on account of the transfer.<sup>3</sup> Finally, it requires employers to inform and consult with employee representatives regarding the effects of the transfer.<sup>4</sup> The Council adopted the directive in response to the increasing number of business mergers, which were affecting workers' job security.<sup>5</sup>

Directive 77/187 exemplifies the gradual involvement of the European Economic Community (EEC) in the social affairs of the member states.<sup>6</sup> The roots of EEC social policy lie in the Treaty of Rome<sup>7</sup> and, more specifically, the Council Resolution of January 21, 1974, in which the Council proposed a social action program.<sup>8</sup> Under this program, the EEC has sought to raise the living and working standards of EEC residents and to harmonize the level of social

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<sup>1</sup> Directive 77/187, Council Directive of 14 February 1977 on the Approximation of the Laws of the Member States Relating to the Safeguarding of Employees' Rights in the Event of Transfers of Undertakings, Businesses, or Parts of Businesses, 20 O.J. EUR. COMM. (No. L 61) 26, 2 Common Mkt. Rep. (CCH) ¶ 3923 (1977) [hereinafter Directive].

<sup>2</sup> *Id.* at art. 3.

<sup>3</sup> *Id.* at art. 4.

<sup>4</sup> *Id.* at art. 6.

<sup>5</sup> [1973-1975 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 9657, at 9457-58 (1974).

<sup>6</sup> See Dubois, *European Social Law*, in *BUSINESS LAW IN EUROPE: LEGAL, TAX AND LABOUR ASPECTS OF BUSINESS OPERATIONS IN THE TEN EUROPEAN COMMUNITY COUNTRIES AND SWITZERLAND* 59 (M. Ellis & P. Storm ed. 1982).

<sup>7</sup> Treaty Establishing the European Economic Community, *done at Rome*, March 25, 1957, 298 U.N.T.S. 3 [hereinafter Treaty of Rome]; see *id.* at arts. 2 (European Community's task is "to promote . . . an accelerated raising of the standard of living"), 117 ("Member States agree upon the need to promote improved working conditions and an improved standard of living for workers"), 118 ("Commission shall have the task of promoting close cooperation between Member States in the social field").

<sup>8</sup> Council Resolution of January 21, 1974, 17 O.J. EUR. COMM. (No. C 13) 1 (1974).

protection guaranteed residents by the member states.<sup>9</sup> The 1974 resolution proposed the enactment of several measures, including one that formed the basis of Directive 77/187.<sup>10</sup>

This Comment explores the scope of Directive 77/187. First, the Comment analyzes the provisions of the directive in terms of their theoretical reach and limits. The Comment then summarizes the opinions of the European Court of Justice interpreting these provisions.

## II. TERMS OF DIRECTIVE 77/187

Because the Council adopted the initiative as a directive rather than as a regulation, each member state must enact national legislation in order for Directive 77/187 to be effective.<sup>11</sup> Article 8 of the directive gives member states two years within which to adopt such legislation.<sup>12</sup> In doing so, member states were free to enact rules more favorable to employees than those dictated by the directive.<sup>13</sup>

The directive's provisions, relating to employer obligations to employees, dismissals, and worker participation, provide employees with significant safeguards in the event businesses are transferred.<sup>14</sup> In several respects, however, the scope of the directive is limited. The safeguards only apply to certain types of business transfers.<sup>15</sup> In addition, even when the directive covers a transfer, its provisions have limited scope.<sup>16</sup> In fact, the directive's terms are less favorable

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*; see 2 Common Mkt. Rep. (CCH) ¶ 3901 (1978).

Since 1974, the Council has adopted two other directives designed to protect the job security of employees. These directives pertain to mass dismissals of workers, Directive 75/129, 18 O.J. EUR. COMM. (No. L 48) 29 (1975), 2 Common Mkt. Rep. (CCH) ¶ 3921 (1978), and to business insolvencies, Directive 80/987, 23 O.J. EUR. COMM. (No. L 283) 23 (1980). A third directive, requiring certain businesses to inform and consult employee representatives before implementing policies affecting employees, has not yet been adopted. See Proposal for a Council Directive on Procedures for Informing and Consulting Employees of Undertakings With Complex Structures in Particular Transnational Undertakings, 23 O.J. EUR. COMM. (No. C 297) 3 (1980). See generally Fera, *The European Economic Community and the Vredeling Proposal: The Debate to Temper Ideology With Realism*, 16 CAL. W. INT'L L.J. 250 (1986).

<sup>11</sup> See Treaty of Rome, *supra* note 7, at art. 189. The member states are free to adopt the methods they deem necessary to achieve the objectives mandated by a directive. *Id.*; see T. HARTLEY, *THE FOUNDATIONS OF EUROPEAN COMMUNITY LAW* 81-82 (1981).

<sup>12</sup> Directive, *supra* note 1, at art. 8(1). At least one member state has failed to enact the required legislation. See *Commission of the European Communities v. Italian Republic*, 1986 E. Comm. Ct. J. Rep. , 4 Common Mkt. Rep. (CCH) ¶ 14,348, at 17,261 (1986).

<sup>13</sup> Directive, *supra* note 1, at art. 7.

<sup>14</sup> *Id.* at arts. 3, 4, 6.

<sup>15</sup> See *infra* notes 20-24 and accompanying text.

<sup>16</sup> See *infra* notes 27-30, 34-36, 40-46 and accompanying text.

to employees than those of two draft versions of the directive proposed by the Commission of the European Communities.<sup>17</sup>

#### A. *Scope*

Article 1 describes the scope of the directive's coverage in broad terms: "This directive shall apply to the transfer of an undertaking, business, or part of a business to another employer as a result of a legal transfer or merger." Although the directive does not define the phrase "legal transfer or merger," the directive's language implies that any change in identity of employers triggers its coverage.<sup>18</sup> In theory, the directive applies to a wide range of business transfers, such as sales, gifts, mergers, and leases.<sup>19</sup>

The directive does not, however, apply to one common type of business transfer, in which a company acquires control of another business without changing that business' corporate structure.<sup>20</sup> In contrast, the draft versions of the directive included these transfers within the directive's scope.<sup>21</sup>

The directive applies to all businesses, regardless of type or size.<sup>22</sup> The only limitation imposed is that the business being transferred must be located within the territory of the EEC.<sup>23</sup> Consequently, the directive does not protect employees of companies located within the EEC that acquire businesses outside the EEC.<sup>24</sup>

#### B. *Safeguards*

Article 3 contains the first of the three safeguards included in the directive. It states that a former employer's rights and obligations arising from an employment contract or employment relationship are transferred to a new employer upon the transfer of the business.<sup>25</sup> Moreover, the directive authorizes

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<sup>17</sup> [1973-1975 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 9657, at 9459 (1974) [hereinafter First Draft Directive]; [1973-1975 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 9775, at 9715 (1975) [hereinafter Second Draft Directive].

<sup>18</sup> See Directive, *supra* note 1, at arts. 2(a) & (2)(b).

<sup>19</sup> Dubois, *supra* note 6, at 73.

<sup>20</sup> Hepple, *Community Measures for the Protection of Workers Against Dismissal*, 14 COMMON MKT. L. REV. 489, 493 (1977).

<sup>21</sup> First Draft Directive, *supra* note 17, at art. 11; Second Draft Directive, *supra* note 17, at art. 1(2); see Hepple, *supra* note 20, at 493.

<sup>22</sup> See Directive, *supra* note 1, at art. 1.

<sup>23</sup> *Id.* at art. 1(2).

<sup>24</sup> See Hepple, *supra* note 20, at 493. Such employees, like employees of acquired businesses, are subject to job insecurity. *Id.* For example, an EEC company buying a non-EEC business may transfer work to the newly-acquired business and dismiss some EEC employees. *Id.*

<sup>25</sup> Directive, *supra* note 1, at art. 3(1).

member states to make the former employer additionally liable after the transfer for the obligations arising from the employment contract or relationship.<sup>26</sup>

The terms of Article 3 impose four limitations on the scope of this provision. First, the new employer is obligated only to a worker who has an employment contract or relationship with the former employer on the date of the transfer.<sup>27</sup> Consequently, an employee who is dismissed or resigns shortly before a transfer cannot invoke the directive's protection. Second, member states may limit the new employer's obligation to respect collective bargaining agreements to a period of one year after the transfer.<sup>28</sup> Third, the new employer does not acquire the former employer's obligations to employees under pension plans.<sup>29</sup> Finally, the directive leaves unclear the status of employees' seniority rights after a transfer. In contrast, the draft versions of the directive specifically protected these rights.<sup>30</sup>

Article 4 provides the second safeguard to employees, stating that a transfer of a business shall not in itself constitute grounds for dismissal.<sup>31</sup> The directive also protects employees from constructive dismissals.<sup>32</sup> A constructive dismissal occurs if substantial, adverse changes in working conditions force a worker to resign.<sup>33</sup>

The strength of these provisions is diminished by two exceptions. First, the prohibition against dismissals does not apply to dismissals made for "economic, technical, or organizational reasons."<sup>34</sup> The directive fails to define this ambiguous phrase. This loophole represents a retreat from the wording included in the draft versions of the directive, which permitted dismissals at the time of transfer only for "pressing business reasons."<sup>35</sup> Second, the directive authorizes member states to designate and exclude categories of employees from the coverage of Article 4.<sup>36</sup>

The final safeguard in the directive mandates that workers participate in decisionmaking at the time of a business transfer. Article 6 requires both the old and new employers to inform employee representatives of the reasons for

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.* at art. 3(2).

<sup>29</sup> *Id.* at art. 3(3). The directive does, however, command the member states to adopt measures to protect the pension rights of present and former employees. *Id.* The first draft of the directive had contained specific provisions safeguarding pension rights. First Draft Directive, *supra* note 17, at art. 9. The Commission decided to replace these provisions with the general language of the final directive because of the intricacies and variations among pension schemes existing in the member states. See [1973-1975 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 9684, at 9518 (1974).

<sup>30</sup> First Draft Directive, *supra* note 17, at art. 6; Second Draft Directive, *supra* note 17, at art. 4.

<sup>31</sup> Directive, *supra* note 1, at art. 4(1).

<sup>32</sup> *Id.* at art. 4(2).

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at art. 4(1).

<sup>35</sup> First Draft Directive, *supra* note 17, at art. 4(1); Second Draft Directive, *supra* note 17, at art. 6(1).

<sup>36</sup> Directive, *supra* note 1, at art. 4(1).

the transfer, the legal, economic, and social implications for employees, and any expected measures that will affect the employees.<sup>37</sup> If the old or new employer does in fact expect changes that will affect employees, the employer must consult with worker representatives.<sup>38</sup> The purpose of these consultations is to attempt to reach an agreement to mitigate these effects.<sup>39</sup>

Article 6 includes four principal limitations to workers' rights to information and consultation. First, if employees have recourse to arbitration to settle disputes, an employer is required to inform and consult employee representatives only if the transfer will likely entail serious disadvantages for a considerable number of employees.<sup>40</sup> Second, employers of workers who do not have representatives need only inform the workers that a transfer is about to take place.<sup>41</sup> Third, Article 6 fails to specify when employers must contact employee representatives, merely providing that employee representatives must be informed "in good time."<sup>42</sup> In contrast, the second draft of the directive required employers to contact workers at least two months before the completion of a transfer.<sup>43</sup> Finally, the directive gives employers the right to decide whether discussions should be initiated.<sup>44</sup> In contrast, the draft versions of the directive required employers to negotiate at the request of employee representatives.<sup>45</sup> The drafts also provided that the representatives could refer disputed matters to binding arbitration if the parties failed to resolve their disagreements within two months.<sup>46</sup>

### III. CASES INTERPRETING DIRECTIVE 77/187

The European Court of Justice, since February 1985, has interpreted Directive 77/187 in five cases. In these cases the court responded to requests for preliminary rulings from national courts.<sup>47</sup> The issues decided by the court fall into two categories. First, the court has considered whether the directive applies to certain types of transfers of businesses. Second, the court has decided the question of whether certain employees are entitled to protection under the directive.

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<sup>37</sup> *Id.* at art. 6(1).

<sup>38</sup> *Id.* at art. 6(2).

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* at art. 6(3).

<sup>41</sup> *Id.* at art. 6(5).

<sup>42</sup> *Id.* at arts. 6(1) & 6(2).

<sup>43</sup> Second Draft Directive, *supra* note 17, at art. 9(2).

<sup>44</sup> See Directive, *supra* note 1, at art. 6(2).

<sup>45</sup> First Draft Directive, *supra* note 17, at art. 8(2); Second Draft Directive, *supra* note 17, at art. 9(3).

<sup>46</sup> First Draft Directive, *supra* note 17, at art. 8(2); Second Draft Directive, *supra* note 17, at art. 9(3).

<sup>47</sup> See Treaty of Rome, *supra* note 7, at art. 177 ("The Court of Justice shall have jurisdiction to give preliminary rulings concerning: . . . (b) the validity and interpretation of acts of the institutions of the Community . . . . Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may . . . request the Court of Justice to give a ruling thereon").

### A. *Types of Transfers within the Scope of the Directive*

The cases in the first category involve businesses which were insolvent or had ceased operations at the time of transfer. In *Abels* a company acquired a business which a court had previously declared insolvent.<sup>48</sup> An employee of the insolvent business who had continued working for the new owner sought recovery of amounts owed him from the insolvent business.<sup>49</sup> The court held the directive does not apply to the transfer of an insolvent business.<sup>50</sup>

The court gave two reasons for its decision. First, it stressed the specific nature of national insolvency laws, as compared with the directive's general terms.<sup>51</sup> In light of this specificity, the court felt that the drafters of the directive would have expressly discussed insolvency if they had intended the directive to cover transfers of insolvent companies.<sup>52</sup> Second, the court believed that a contrary ruling might undermine the directive's objective of promoting job security.<sup>53</sup> A company considering the acquisition of an insolvent business might decide not to do so if it would be forced to assume all of the insolvent company's obligations to its employees.<sup>54</sup>

Although the directive does not apply to insolvent businesses, the court ruled that it does encompass transfers of businesses in less serious financial straits.<sup>55</sup> The court held that the directive's provisions apply to a company granted a *surséance van betaling*, or judicial leave to suspend payment of debts.<sup>56</sup> The court distinguished the less serious financial condition of such companies from that of insolvent businesses.<sup>57</sup>

In *Spijkers* the court considered whether the directive applies to a company which had completely ceased operations before selling its assets to another company.<sup>58</sup> The acquiring company used the assets to carry on a similar business.<sup>59</sup> It hired most of the defunct company's employees, excluding the plaintiff, who sought reinstatement to his former position.<sup>60</sup> The court declined to

<sup>48</sup> H.B.M. *Abels v. Admin. Bd. of the Bedrijfsvereniging voor de Metaalindustrie en de Electrotechnische Industrie*, 1985 E. Comm. Ct. J. Rep. 469, [1983-1985 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 14,176, at 16,071 (1985).

<sup>49</sup> *Id.*

<sup>50</sup> *Id.* at 16,075.

<sup>51</sup> *Id.* at 16,072.

<sup>52</sup> *Id.* at 16,073. In fact, other directives have specifically considered the status of insolvent companies. *Id.* at 16,072.

<sup>53</sup> *See id.* at 16,073.

<sup>54</sup> *Id.*

<sup>55</sup> *Id.* at 16,074.

<sup>56</sup> *Id.* at 16,075.

<sup>57</sup> *Id.* at 16,074.

<sup>58</sup> *Jozef Maria Antonius Spijkers v. Gebroeders Benedik Abattoir C.V.*, 1986 E. Comm. Ct. J. Rep. 4 Common Mkt. Rep. (CCH) ¶ 14,298, at 16,853 (1986).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

rule as a matter of law whether the directive applied to this type of transfer.<sup>61</sup> Rather, it stated that the decisive criterion in such cases is whether the business retains its identity.<sup>62</sup> The court, in focusing on this criterion, reasoned that the directive only seeks to ensure the continuity of employment relationships in ongoing businesses.<sup>63</sup> Whether or not a transferred business is a going concern, subject to the directive, is a matter of fact.<sup>64</sup>

### B. *Employees Entitled to Protection*

In three cases the court has considered whether the directive protects certain employees of businesses covered by the directive.

In *Botzen* a company acquired only a portion of another business.<sup>65</sup> Employees of a department of that business that was not acquired sought a ruling that their employment relationships with their former employer were automatically transferred to the new company.<sup>66</sup> The court, in rejecting this position, reasoned that an employment relationship is characterized by a link between an employee and the part of the business in which the employee works.<sup>67</sup> The court implied that the directive did not cover the plaintiffs, since the new employer did not acquire their department.<sup>68</sup>

In *Wendelboe* a failing business dismissed most of its employees one month before another company acquired the business.<sup>69</sup> The employees sued their former employer for damages for unlawful dismissal and unpaid vacation pay.<sup>70</sup> In defense, the employer argued that it had transferred to the acquiring company its obligations to the employees.<sup>71</sup> The court rejected this argument, noting that the directive refers only to the transfer of employment relationships existing on the date of transfer.<sup>72</sup> Moreover, the directive's goal of ensuring that such

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<sup>61</sup> See *id.* at 16,854–55.

<sup>62</sup> *Id.* at 16,854.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.* Factors to be considered include the type of business, the degree of similarity of business activities, the period during which activities were suspended, whether and to what extent customers, employees, and tangible assets of the business were transferred, and the value of the business' intangible assets. *Id.*

<sup>65</sup> *Arie Botzen et al. v. Rotterdamsche Droogdok Maatschappij B.V.*, 1985 E. Comm. Ct. J. Rep. 519, [1983–1985 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 14,178, at 16,078–79 (1985).

<sup>66</sup> See *id.* at 16,079.

<sup>67</sup> *Id.* at 16,080.

<sup>68</sup> See *id.*

<sup>69</sup> *Knud Wendelboe et al. v. L.J. Music ApS*, 1985 E. Comm. Ct. J. Rep. 457, [1983–1985 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 14,179, at 16,082 (1985).

<sup>70</sup> *Id.*

<sup>71</sup> See *id.*

<sup>72</sup> *Id.* at 16,083–84.



relationships remain unchanged upon a change of employers does not apply where workers leave a company's employ before a transfer occurs.<sup>73</sup>

Finally, the court in *Danmols Inventar* addressed a situation where an employee of a transferred business was a major stockholder and chairman of the board of directors of the acquiring company.<sup>74</sup> The court considered two issues relating to this atypical situation. First, it decided whether the directive protects an employee who freely chooses not to be an employee of the acquiring company.<sup>75</sup> It then considered whether in fact a worker who holds a significant ownership interest in an acquiring company is an "employee" of that company within the meaning of the directive.<sup>76</sup> The court ruled that the directive does not apply to employees who choose not to continue as employees of the new employer, since the directive's protection is unnecessary in such cases.<sup>77</sup> The court, however, declined to resolve the second issue, leaving it to each member state to define "employee" for purposes of the directive.<sup>78</sup>

#### IV. CONCLUSION

With the adoption of Directive 77/187 the EEC has furthered its goal of raising and equalizing the living standards of employees in the member states. The terms of the directive, while more limited in scope than the draft versions of the legislation, provide safeguards not previously enjoyed by many EEC workers.

The recent decisions of the European Court of Justice interpreting the directive distinguish various types of business transfers and employees. The directive covers some, but not all, transfers of financially troubled companies. Employees of covered businesses must have an employment relationship with a transferred part of the business at the time of transfer and must continue to work for the new employer in order to invoke the directive's safeguards.

Thus, the directive increases the safeguards given to employees of transferred businesses. Despite this protection, the directive contains restrictive language and has not been consistently interpreted by the European Court of Justice. Consequently, EEC employees will have to look to other EEC directives for more complete protection against the negative consequences of business transfers.

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<sup>73</sup> *Id.* at 16,083.

<sup>74</sup> *Foreningen af Arbejdsledere i Danmark v. Danmols Inventar A/S*, 1985 E. Comm. Ct. J. Rep. , 4 Common Mkt. Rep. (CCH) ¶ 14,227, at 16,373 (1985).

<sup>75</sup> *Id.* at 16,374-75.

<sup>76</sup> *Id.* at 16,374.

<sup>77</sup> *Id.* at 16,375.

<sup>78</sup> *Id.* at 16,376.