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Has the so-called “Work Law” made dismissals on economic grounds more secure?

In our October 2016 e-newsletter, we addressed *forfait* working time arrangements, an important element of the so-called “Work Law” of August 8, 2016[1]. This month, we will focus on an even more sensitive issue raised by said Law: Dismissals on economic grounds.

It is clear that through successive reforms, the French legislator, navigating by sight on troubled waters and finding himself in the middle of a power game between trade-unions and employers’ federations, has been trying to reach his goal to make French labor and employment law more secure while maintaining focus on employment protection and growth. In this spirit, the Work Law attempts to make dismissals on economic grounds more secure but, after so many compromises, it does not really recast the existing set of rules and even creates additional uncertainties. As such, it seems that unfortunately the hopeful resolution to build a secured framework adapted to economic and financial constraints has not been yet fulfilled.

The Work Law brings about two essential changes with respect to dismissals on economic grounds. It first

tries to clarify the legal definition of "economic grounds" that can be relied upon to justify a dismissal. In addition, it lifts – in a certain specific case – the prohibition imposed by French courts on the seller of a business to proceed with dismissals before transferring such business.

I. The changes brought about by the Work Law with respect to the definition of "economic grounds"

The provisions of the Work Law concerning dismissals on economic grounds will enter into force on December 1, 2016.

1. Codification of economic grounds acknowledged by French courts as likely to justify a dismissal

Before the adoption of the Work Law, only two economic grounds were codified: Article **L. 1233-3** of the French Labor Code defined a dismissal on economic ground as a dismissal "*decided by the employer for one or more reasons that are not related to the employee, resulting from the elimination or transformation of an employment position, or a modification, refused by the employee, of an essential component of the employment contract, due, notably,* ***to economic difficulties or technological changes***".

The *Cour de Cassation* (French Supreme Court) had also laid down two other economic grounds that could be relied upon to justify a dismissal: **The discontinuation of the company's operations[2] and the reorganization of the company in order to safeguard its competitiveness[3]**.

To clarify things, the Work Law makes dismissals on economic grounds a bit more secure by including in the French Labor Code the two economic grounds established by French courts.

These two grounds are incorporated into Article L. 1233-3 just after the legal grounds, i.e. economic difficulties and technological changes.

It should be noted that, as before, the list of economic grounds set in the French Labor Code is not exhaustive. The adverb "notably" has been maintained and, as such, French courts will be entitled, where appropriate, to consider other situations.

As the Work Law codified the economic grounds set by French courts without providing any further clarification or detail, judges will probably maintain the requirements that they have previously laid down to be entitled to rely on these grounds for dismissal. For example, the need to safeguard competitiveness may not be invoked only to make additional profits[4] and the discontinuation of the company's operations must not result from the employer's reprehensible carelessness[5].

2. The concept of "economic difficulties" is clarified

A main innovation introduced by the Work Law is the attempt to create an automatic mechanism to ascertain the existence of economic difficulties by providing indicators aimed at establishing such economic difficulties more objectively.

As such, pursuant to Article L. 1233-3 of the French Labor Code, in its new version applicable as from December 1, 2016, economic difficulties *"are characterized by the significant alteration of at least one economic indicator such as:*

- *a decline in orders;*
- *a decline in turnover;*
- *operating losses;*
- *a deterioration of cash flow;*
- *a deterioration of EBITDA;*
- *any other element which can justify these difficulties"*[6].

As the list is not static, judges have the possibility to complement it with other types of economic difficulties.

In addition, the legislator has added a key criterion that was not included in the original Bill, i.e. the "significant alteration" requirement.

More specifically, with regard to the significant decline in orders or in turnover, Article L. 1233-3 of the French Labor Code, in its new version, provides a highly detailed definition:

"A significant decline in orders or turnover is established wherever the duration of this decline is, compared with the same period of the preceding year, at least equal to :

- *a quarter for a company with less than eleven employees;*
- *two consecutive quarters for a company with at least eleven but less than fifty employees;*
- *three consecutive quarters for a company with at least fifty but less than three hundred employees;*
- *four consecutive quarters for a company with three hundred employees or more"*[7].

These details should not be taken lightly and raise some questions. Indeed, the decline in orders or in turnover is not quantified. Consequently, a slight alteration should not be sufficient to justify a dismissal on economic grounds; otherwise this would mean that this ground for dismissal is merely based on a time criterion.

In addition, the comparison with the same period of the preceding year is problematic as the decline can follow an exceptional increase in orders or in turnover. In other words, the decline should in fact be put into

perspective.

One could also legitimately wonder about the relevance of the definition of economic difficulties when significant difficulties, e.g. a decline in turnover during four consecutive quarters, are invoked. The adjective "consecutive" may be tricky. For example, if the turnover of a large company falls by 30% from year to year, such company will not, in principle, be entitled to proceed with economic dismissals if it has "by misfortune" recorded a positive quarter between two or three negative quarters!

While the effort to clarify the definition of the "economic grounds" is welcome, there is a concern that the new indicators laid down by law will trigger further discussions before French courts and continue to fuel the abundant line of decisions on dismissals on economic grounds.

Furthermore, it is regrettable that the legislator backed off on its initial plans to restrict the geographical scope of assessment of the economic ground to the national territory only wherever the company that contemplates dismissing employees on economic grounds is part of a global corporate group.

As a result, the economic ground will still be assessed at the level of the business sector of the group to which the company belongs, as opposed to the business sector that is common only to the companies of the group which are established on the French territory[8].

In this respect, two very recent decisions handed down on November 16, 2016[9] by the *Cour de Cassation* enshrined the principle according to which the economic ground must be assessed at the level of the group to be understood as a set of companies under the control or the influence of a dominant company. In one of these two cases, the *Cour de cassation* approved the approach adopted by the Court of Appeals that, in order to assess whether the ground put forth to dismiss 12 employees was "real and serious", had examined not only the situation of the employer but also the situation of the holding company based in Norway and the situation of other affiliated companies that operate in the same business sector.

This outcome is quite regrettable. Indeed, it is not because a global group makes profits that it must maintain failing companies without limitation of time. The *Cour de Cassation*'s line of decisions on this issue is difficult to understand for companies, and also primarily for foreign investors, and, to the best of our knowledge, does not exist in any other country around the world.

II. The Work Law restricts the prohibition to dismiss employees prior to the transfer of a business when said business is to be taken over

The transfer of a company, and more generally the transfer of an autonomous economic entity, automatically entails the transfer of the related employments agreements from the seller to the purchaser, as per Article L.1224-1 of the French Labor Code and, traditionally, dismissals on economic grounds implemented by the

seller in connection with such a transfer are ineffective.

As such, the successive employers may not, in principle, agree to implement a certain number of dismissals before the completion of the transfer in order to limit the number of the to-be-transferred employees[10].

However, purchasers frequently require that a lay-off plan be implemented prior to the contemplated transfer. The risks related to the circumvention of the principle of automatic transfer of the employment agreements (i.e. nullification of the dismissals and significant claims for damages) generally discourage many potential purchasers who are willing to give a new chance to a failing business but who have not the capacity to take over all the employees.

Article 94 of the Work Law [11] thus displays a cool pragmatism by creating an exception to the aforementioned principle, but only in a very specific case.

The exception provided for in the last paragraph of new Article L. 1233-61 of the French Labor Code can only apply in the following specific case:

– closure of an establishment that entails collective dismissals for economic grounds leading to the implementation of a so-called *Plan de Sauvegarde de l'Emploi* (i.e. collective lay-off plan),

– affecting a company that has at least 1,000 employees, that belongs to a group that has at least 1,000 employees or that belongs to an EU-scale group[12].

In fact, this exception is available to companies that would be willing to accept a purchase offer under the obligation to search for potential purchasers imposed by the famous *Florange* Law.

As such, this exception can only come into play in specific situations where the non-completion of a transfer would entail the closure of the company.

These provisions shall apply to procedures for dismissals on economic grounds initiated since the publication of the Work Law, i.e. August 9, 2016.

While this measure is welcome and will facilitate the taking over of companies under the legislative framework created by the Florange Law, it is again regrettable that the legislator remained so timid and did not decide to broaden this exception to include smaller businesses (that do not belong to a large group / EU-scale group). It could be considered that there might be a breach of equality as small- and medium-sized businesses forced to implement a collective lay-off plan and to envisage closing down are not entitled to agree with a potential purchaser for the taking over of the business with only part of the employees. Of course, the last solution is to sell off the assets during public auctions held at a court of law wherever judicial receivership or liquidation proceedings have been initiated, subject, however, to proving that the relevant company has filed with the commercial court a so-called "declaration of cessation of payment"… which is quite a worst case scenario for a company.

[1] Law of August 8, 2016 on Work, Modernization of Social dialogue and Securing Professional Careers

[2] Labor Chamber of the Cour de Cassation, January 16, 2001, n° 98-44.647; Labor Chamber of the Cour de Cassation, November 16, 2011, n°11-40.071

[3] Labor Chamber of the Cour de Cassation, April 5, 1995, n° 93-42.690

[4] Labor Chamber of the Cour de Cassation, February 22, 2006, n° 04-40041

[5] Labor Chamber of the Cour de Cassation, January 16, 2001, n° 98-44647

[6] Article L.1233-3 of the French Labor Code, as amended by the Work Law

[7] Article L. 1233-3 of the French Labor Code, as amended by the Work Law

[8] Labor Chamber of the Cour de Cassation, June 26, 2012 n° 11-13.736, Labor Chamber of the Cour de Cassation, June 12, 2001, n° 99-41.571

[9] Labor Chamber of the Cour de Cassation, November 16, 2016 n°14-30063 and n°15-19327

[10] Labor Chamber of the Cour de Cassation, January 20, 1994, n°90-432350

[11] Article 94 of the Work Law

[12] These are companies subject to the obligation to offer a congé de reclassement (redeployment leave) provided for under Article L. 1233-71 of the French Labor Code