

Employment & Labour - Poland

New approach to non-compete compensations for self-employed contractors

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[Introduction](#)
[Case study](#)
[Other rulings](#)
[Comment](#)

Introduction

It is common practice in Poland for companies to hire individuals based on civil law contracts (ie, those for self-employed contractors), as opposed to employment agreements. In many cases, the decision to use such a framework is caused by the more favourable tax and social security treatment of proceeds from such contracts, as well as the greater flexibility than in traditional employment relationships.

However, one practical issue concerning the structure of cooperation between companies and self-employed persons is whether remuneration should be stipulated in return for an obligation to refrain from competitive activity for a certain period after completion of the relationship between the parties (assuming that the introduction of such an obligation is at all permissible); and, if so, how to determine the amount of such remuneration.

On December 5 2013⁽¹⁾ the Supreme Court issued a ruling on the issue of compensation for a self-employed individual in return for a post-termination non-compete obligation.

Case study

Facts

The claimant (the company) and the defendant (an individual performing services for the benefit of the claimant) had been parties to a services contract. In the contract, the defendant committed to keep information obtained in connection with performing the contract confidential, as well as to refrain from competitive activity for the term of the contract and for one year following the termination of employment.

The contract provided for no compensation in return for the aforementioned obligations, although it did provide for liquidated damages (ie, a contractual penalty) for the claimant if the defendant breached the obligations. The liquidated damages were set at 10 times the defendant's average remuneration under the contract, calculated over the previous six months.

The defendant violated the non-compete obligation before one year had elapsed from the termination of employment and the claimant demanded payment of the liquidated damages.

Decision

The Supreme Court upheld the lower court decisions, which awarded the liquidated damages to the claimant.

The court disagreed with the defendant, who argued that the services contract with a gratuitous non-compete obligation had been made in breach of law. In particular, the court held that the contract was not contrary to the nature of the legal relationship between the parties (which is one of the statutorily introduced limitations of freedom of contract).

According to the court, the fact that services contracts are not regulated in detail in the statutory provisions of law evidences the legislature's will to introduce a broad scope to freedom of contract, thus enabling the contracting parties to adjust the services contract to the business needs and their individual interests. A post-termination non-compete clause that does not provide for compensation and is secured with liquidated damages

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is not deprived of its business rationale and is in line with the general rule for civil contracts in business relations.

Other rulings

Gdańsk Court of Appeal ruling

In another 2013 court ruling, issued by the Gdańsk Court of Appeal on May 14 2013,⁽²⁾ a different conclusion was reached.

The court was asked to resolve a dispute concerning the payment of liquidated damages between the claimant (a company commissioning transportation services) and the defendant (an individual conducting business activities, performing transportation services for the claimant). The contract for transportation services between the parties provided for a two-year non-compete obligation, secured with liquidated damages of €50,000, without any right to compensation stipulated in favour of the defendant.

After termination of the cooperation (which had been in force for a short period only), the claimant demanded payment of the liquidated damages, on account of the fact that the defendant was performing services for the claimant's competitor, with which the defendant had begun cooperating even before he started to work for the claimant.

The court found that the non-compete clause was unenforceable, as it contradicted the rules of social cohabitation (a general rule of the civil law). The court emphasised that a contract's compliance with the rules of social cohabitation should be examined on a case-by-case basis. It is therefore not possible to define universal rules applicable to each situation. However, the following examples of possible violations of these rules have been indicated:

- exorbitant violation of equity rules;
- violation of the rule of equivalence, leading to a severe disadvantage for one of the parties;
- exorbitant disproportion of benefits;
- restriction of one of the parties' business activity;
- violation of the rules of a fair business; and
- loyalty towards the other party.

In this case, the court stated (among other considerations) that the liquidated damages had put the defendant at a severe disadvantage by restricting his freedom to conduct business in a manner that was disproportionate to the purpose of the protection and the length of the parties' cooperation. Moreover, the lack of equivalent compensation violated the principle of fairness.

According to the court, there is no rule that a post-termination non-compete covenant in relations between professionals (entrepreneurs) with no provision for compensation will comply with the law. The court did acknowledge that there are no grounds to implement solutions set forth in the Labour Code where compensation for a post-termination non-compete obligation is mandatory in civil law relationships. Nevertheless, it found that a lack of proper compensation in a civil law relationship may lead to a violation of freedom of contract and render the clause invalid.

The court stressed that in order to declare a contract contrary to the rules of social cohabitation, a disproportion in the parties' performances is insufficient; rather, a gross disproportion is required (which was present in the case at hand).

Supreme Court ruling

The Supreme Court took a similar position in its ruling of September 11 2003.⁽³⁾ The defendant was an individual conducting business activity who had committed to perform no competitive activities for three years following termination of the mandate agreement with the claimants (partners in a partnership).

Under the agreement, the defendant was entitled to no compensation for adhering to the non-compete obligation. The obligation was secured by liquidated damages of PLN100,000 (approximately €23,000) for breach of the non-compete obligation. The Supreme Court deemed the defendant's commitment contrary to the rules of social cohabitation due to the lack of equivalent performance stipulated for the benefit of the defendant.

Comment

In its new December 2013 ruling, the Supreme Court took a completely new approach to post-termination non-compete covenants in civil law relationships involving self-employed contractors. It emphasised that the independence of the two professionals in stipulating the conditions of their cooperation is very broad. The Supreme Court also stressed that courts should interfere with entrepreneurs' decisions to shape their cooperation only in exceptional cases.

Nevertheless, as the general rules concerning freedom of contract apply to non-compete agreements between entrepreneurs, the individual assessment of each case in future rulings of common courts is expected, rather than strict adherence to the latest approach. Post-termination non-compete covenants for self-employed contractors should still be carefully formulated, in light of the particular circumstances. In certain situations, such covenants (if not coupled with appropriate remuneration) could potentially still be undermined.

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Endnotes

- (1) V CSK 30/13.
- (2) I ACa 174/13.
- (3) III CKN 579/01.

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