SZECSKAY
ÜGYVÉDI IRODA - ATTORNEYS AT LAW

H-1055 BUDAPEST, KOSSUTH TÉR 16-17
(MAIL: H-1245 BUDAPEST PF/POB 1228)
HUNGARY

TEL: +36 (1) 472 3000 • FAX +36 (1) 472 3001 • INFO@SZECSKAY.COM • WWW.SZECSKAY.COM

NON-COMPETITION AGREEMENT FROM THE PERSPECTIVE OF HUNGARIAN LABOUR LAW

In this article, we provide a brief overview of a non-competition provision in an employment agreement undertaken for a period after termination of the employment agreement, from the perspective of the Labour Code. It is worth addressing if and how the parties may deviate from the provisions of the Labour Code governing non-competition agreements.

Parties concluding an employment agreement sometimes wish to conclude a non-competition agreement as well, which obliges the employer to refrain from *e.g.* accepting an employment at a competitor of the former employer for a certain period of time. Therefore, it is important to know and understand the relevant provisions of the Labour Code concerning such non-competition agreements. In general, the parties may deviate from the rules laid down in the Labour Code to the benefit of the employee. At the same time, there are also provisions from which the parties may not deviate. Furthermore, there are certain provisions from which the parties may deviate even to the detriment of the employee. We will address below the provisions of the Labour Code on non-competition agreements from the perspective of ordinary and executive employees. We will also briefly touch upon the relation between collective labour agreements and non-competition agreements.

1. General rules: length and compensation

The Labour Code provides that based on the agreement by the employer and the employee, an employee may – for a period of a maximum of two years after termination of the employment – not engage in any conduct which jeopardizes or intervenes with the employer's rightful business interests. The employer must pay appropriate consideration in exchange for the non-competition undertaking. When it comes to determining the amount of appropriate compensation, one must examine particularly the extent to which the non-competition agreement prevents the employee from getting a new job and also take into account his/her qualification and experience. The amount of appropriate compensation may not be less than one-third of the employee's basic wage, payable for a period equal to the length of the non-competition period. We note that this amount is only a minimum amount and that the stricter the non-competition undertaking, the higher the amount which has to be paid as compensation.

It is also worth noting that the Labour Code no longer stipulates that the non-competition agreement is subject to the provisions of the Civil Code. Therefore, such an agreement may

not be challenged on grounds of the considerations being considerably disproportional. However, if the compensation paid as consideration for the non-competition undertaking is not appropriate, the agreement may be partially invalid. In this case, courts may either require the employer to pay to the employee an appropriate compensation in exchange for the non-competition undertaking, or declare that the entire agreement is null and void.

2. The employee's rescission right

In addition to the maximum period of a non-competition undertaking and the amount of appropriate compensation, the employee may rescind (*i.e.* unilaterally terminate with retroactive effect) the non-competition undertaking if he/she terminates his/her employment with immediate effect by way of extraordinary termination notice. Under Hungarian law, an employer or employee may terminate an employment relationship by extraordinary termination notice in the event that the other party

(i) willfully, or by gross negligence, commits a grave violation of a substantive obligation arising from the employment relationship; or
(ii) otherwise engages in a conduct rendering the maintenance of the employment relationship impossible.

Of course, the parties are free to grant a rescission right to the employee in other cases too. Furthermore, it is worth noting that an executive employee's employment agreement and, respectively, a collective labour agreement may deviate from the provision granting a rescission right to the employee even to the employee's detriment. In other words, a collective labour agreement may stipulate that said rescission right does not apply. (We note that collective labour agreements typically do not contain any non-competition undertaking.) A non-executive employee's employment agreement may, however, not lawfully deprive the employee of the rescission right.

3. Questions of legal succession

The Labour Code makes it clear that in the event that there is a legal succession on the employer's side, the rights and obligations of the employer concluding the non-competition agreement will pass on to the new employer. Including such a provision in the Labour Code was necessary because judicial practice has not been authoritative as to whether the rights and obligations laid down in a non-competition agreement would pass on to a new employer that happens to be a legal successor of the former employer. An employment agreement or – most probably– also a collective labour agreement may not lawfully stipulate that in case of a legal succession on the employer's side, the rights and obligations of the employer concluding the non-competition agreement will not pass on to the new employer. Based on the Labour Code, deviation is theoretically allowed in case of an executive employee, however, it remains to be seen in the future whether this interpretation will be accepted by courts.

4. Other considerations concerning deviating from the Labour Code

It is also worth noting that, under the Labour Code, the employment agreements of executive employees (*e.g.* managing directors and those employees working under the direct control of the managing director, who may partially or fully substitute the managing director) may deviate from the provisions of the Labour Code, governing employment relationships, with the only exception that they cannot deviate from the provision which provides that collective labour agreements are not applicable to executive employees. This seems to suggest that in case of executive employees, deviation is allowed from the provisions of the Labour Code governing non-competition undertakings. However, if the non-competition agreement is not regarded as part of the employment agreement, but rather as a separate agreement, the conclusion may also be that no deviation is allowed from the provisions governing non-competition agreements. It seems that the question of whether the parties may deviate from the provisions of the Labour Code governing non-competition agreements will need to be interpreted and decided by the court.

As for non-executive employees, it is certain that the parties may not deviate from the maximum length of the non-competition period and, respectively, the minimum amount payable as consideration for the non-competition undertaking to the employee's detriment, i.e. no non-competition period longer than two years and/or an amount less than one-third of the employee's basic wage as appropriate compensation may be lawfully stipulated in either an employment agreement or - most probably - also in a collective labour agreement.

In addition to the above, it is also worth mentioning that if the employer fails to pay an appropriate compensation to the employee in consideration for the non-competition undertaking, the employee is not bound by the non-competition undertaking. At the same time, if the employee fails to comply with the non-competition obligation, the employer may reclaim the full amount paid to the employee for undertaking the non-competition obligation.

****

Zoltán Balázs Kovács (zoltan.kovacs@szecskay.com)

Tel: +36 (1) 472 3000 • Fax +36 (1) 472 3001 • www.szecskay.com