1 Introduction

A company’s decision to employ a person can be viewed as an investment-decision. A decision to educate or train an employee to improve his or her skills can also be regarded as an investment-decision by the company.

All investments involve risk. A successful investment can gain considerable profit for the company and it constitutes a valuable asset. The company therefore has an interest in protecting its investments. An asset which from one day to another can vanish from the company or – which is worse for the company – can be transferred free of charge to a competitor provides a high risk. If, on the other hand, an investment for some reason proves to be a failure in one way or the other, the company usually wants to reallocate its investments as soon as possible to reduce its losses. An investment which is not profitable or which generates losses provides a high risk, when the company has few options to bring the investment to an end.

When an investment constitutes of a mutual business contract, the normal way of handling and calculating risk for both parties is by contractual provisions. Through provisions in their contract, supplemented by the legal framework the society provides, they distribute the risk that is involved in the investment. Freedom of contract makes it easier to distribute and thereby calculate and manage risk.

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Labour legislation\(^1\) normally restrains freedom of contract. The legislation is not primarily aimed at promoting and protecting companies’ investments and their use of capital. Instead it has a social-protective character. There is in countries like Sweden a wide consensus that the employment contract for social and human reasons should not entirely be governed by the principle of freedom of contract.

There are thus good reasons for special protective legislative measures with respect to the employment relationship. But the company, i.e. the employer, must nevertheless pay attention to labour legislation in order to calculate and manage the risk that employment relationships provide. This paper deals with some aspects of the impact of labour legislation on primarily small and medium sized companies’ possibilities to calculate and manage risk. The perspective is that of the company, but it should be borne in mind that the difficulties for the company to calculate the economic risk arising from labour legislation can be – and often is – justified and balanced by advantages of social and human nature that the legislation provides the employees. The examples of the law are mainly taken from Swedish law.

2 Protecting the investment in the employment relationship

The procedure to employ the right person can take a long time and cost a lot of money for the company.\(^2\) To employ a person can, especially in small companies, be a very important decision, a decision which must be thoroughly prepared.

If the employed person does not show up when the employment starts or if he quits soon after he has entered into the employment relationship, the ef-

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1 Labour legislation is a broad concept. This paper concentrates on legislation aimed at protecting employment and promoting worker’s participation in the employer’s decisions. I have for the purpose of this paper not felt the need for a more precise definition than that.

2 When considering the administrative costs for hiring a person the obligations laid down by EC-Directive 91/533/EEC on an employer’s obligation to inform employees of the conditions applicable to the contract or employment relationship must be observed.
fort and money that were laid down in finding that person are immediately lost.

A regular, open-ended employment contract is a long-term contract. The tasks that an employee has to perform over the years in accordance with the employment relationship varies due to, for example, technical, organisational or economic reasons. The company therefore normally has to train and educate the employee in the course of the employment relationship. A newly employed person also needs some training before he can perform his tasks effectively. Training and education can be expensive for the company. The money put up by a company to train and educate an employee can at the same time increase the employee’s ”market-value” and make him more attractive to competitors.

The company has an interest in keeping the employee until at least the investment in the employment-procedure and/or training and education is paid off by the work the employee has performed for the company. If the employee quits before the ”pay-off-period” has elapsed, the investment is a financial failure. Even if the ”pay-off-period” has elapsed, the company has, in order to keep a competitive edge, an interest in keeping its trained and educated employees from transferring to a competitor.

In Sweden an employee who is employed under an open-ended contract can quit anytime he likes. He must not have or state any valid reason for the termination of the employment contract, but he has to observe a period of notice. Only if the employer has to a considerable extent disregarded his obligations to the employee is the employee free to leave his employment immediately. If the employee does not show up at the work place, the employer can not by legal means force the employee to come back and finish the work, not even for the applicable period of notice; the courts or the police can not be used to force an employee to actually perform the agreed work.

If the employment contract is one of fixed duration or for a specific task, the main rule is that the employee is free to leave only when the agreed period has elapsed or the task is finished. For that period the employer can be fairly sure of having access to the employee. Only under special circumstances can the employee (or the employer) bring the employment relation-
ship to an end before the agreed period has elapsed. It is also possible to conclude an employment contract that has a definite end-point, but for other purposes runs until further notice and therefore can be terminated after a period of notice by either party anytime before the maximum-period has elapsed; the contract is then open-ended with a definite end-point.

In Sweden it is allowed to conclude an employment contract for a fixed duration only in those cases enumerated in the legislation; through collective agreements it is possible to limit or extend the right to conclude an employment contract of fixed duration. The company therefore normally has to use open-ended employment contracts, and, when it is allowed, the contract for a fixed duration represents only a temporary investment for the company.

Apart from using employment contracts of fixed duration the company can use different strategies to minimise the risk that the investment in an employment relationship is brought to nothing due to the fact that the employee is using his right to terminate the employment relationship at will. One strategy is, of course, to satisfy the employee in various ways in order to keep him from exercising his right.

Another strategy is to minimise the amount of the investment for the company in order to reduce the company’s financial risk. The key here is to get someone else to pay the bill. The company can try to attract well educated and productive employees from other companies. A popular way of reducing the costs for employment and training and education is to let the state pay. Hiring-costs can be reduced by using free public employment services. There are also often various state programmes for training and educating young or unemployed persons.

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3 See the report "Ny anställningsskyddslag" (SOU 1993:32), at p. 425 ff., from a Swedish governmental committee on labour legislation and statements made by the Swedish National Labour Court in the cases AD 1979 nr 152, 1991 nr 36 and 1991 nr 81.


5 See regarding ILO the 1948 Employment Service Convention (no. 88). Compare also the 1949 revised Fee-Charging Employment Agencies Convention (no. 96). As of 4th June 1993 Sweden is, after termination, no longer bound by the latter convention (see the Bill 1991/92:89).
The employee must normally observe a period of notice when he wants to quit. According to the Swedish legislation the period of notice is at least one month. But the employer and the employee can agree on a longer period of notice; it is also possible to prescribe a longer (or shorter) period of notice in a collective agreement. One way of, temporarily, protecting the investment in the employment relationship is hence to use a long period of notice in the employment contract. Another mechanism to achieve the same result is to agree that an open-ended employment contract may not be terminated by the employee until a certain period of time has elapsed; such a provision is probably valid according to Swedish law. The effect of provisions on the length of the period of notice or on a minimum length of service can be strengthened by prescribing certain (high) penalties for breach of such provisions.

In Sweden such provisions as those now mentioned seem to be in use to some extent. The length of the ”binding-period” seems, however, to be rather short in most cases, a couple of months rather than a year or more. The provisions have not generated any case law worth mentioning. It must be regarded as uncertain whether a very long binding-period – or very harsh penalty-provisions – will be upheld. It can be argued that provisions on a longer binding-period are more likely to be accepted if the provisions are justified by and connected to a specific action on the employer’s side, for example a substantially increased salary or an expensive and attractive education paid for by the employer. It is probably of importance whether the binding-period is mutual or unilateral. In Finland and in Norway the length of the period of notice for the employee may not exceed that of the employer.

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6 See § 11 of the Employment Protection Act. According to the Norwegian and Finnish legislation the period of notice is at least one month but can be longer depending on the length of service, see, for Norway, § 58 of the 1977 Act on Worker Protection and Working Environment (Lov 4. februar 1977 nr. 4 om arbeidervern og arbeidsmiljø m.v.) and, for Finland, § 38 of the 1970 Act on Employment Contract (Lagen 30.4.1970 om arbetsavtal [320/70]).
8 Compare AD 1993 nr 184.
9 Compare for a special case (air-force pilots) AD 1991 nr 38 and 1992 nr 67.
10 In Finland the maximum length of the period of notice is six months.
11 The same rule exists also in, for example, Germany, see § 622 (5) of the Civil Code (Bürgerliches Gesetzbuch, BGB).
During the time when the employment relationship is in effect the employee has to be loyal to his employer. This is one of the characteristics of the employment relationship. The employee must not engage in any activity in competition with the employer’s activities, and if he does the employer is entitled to terminate the employment relationship, at least if the employer observes the period of notice.\(^\text{12}\) It is clear that the company during the time when the employment relationship is in effect has a legal right – emanating from the contractual relationship itself – to prevent its employees from using their skills for the benefit of competitors.\(^\text{13}\) But if the employee quits, the main rule is that the employer can not, after the employment relationship has ended, prevent the employee from using his or her acquired skills for a competitor. Non-competition provisions are, however, allowed in employment contracts. The provisions may not be extended further than what can be deemed as reasonable.\(^\text{14}\) In order to determine what is reasonable the courts seeks – in accordance with the legal history – guidance in an agreement concluded in 1969 by the largest employer’s organisation and three leading trade unions for privately employed white-collar workers. There must be a specific need for non-competition provisions, and the binding-period shall not normally exceed two years. The penalty for breach of the provisions shall normally be restricted to the equivalent of six month’s pay.\(^\text{15}\) A non-competition provision, temporarily restricting the employee’s possibilities to use his or her particular skills on the appropriate labour market, can in itself refrain the employee from quitting.

**Summary** Freedom of contract is not generally restricted with respect to the company’s possibilities to prevent employees from quitting and thereby protecting the investment in the employment relationships. Provisions that in effect prescribe a certain binding-period for the employee seem in principle to be legally valid, but the provisions, or the sanction for a breach of

\(^{12}\) See for example the cases referred to in Sören Öman "Anställningsskyddslagen – Sammanställning av rättspraxis" [1993] at p. 130 ff.

\(^{13}\) If the employment relationship is terminated by mutual agreement, there may be some remaining loyalty-obligations, see statements in AD 1993 nr 41.

\(^{14}\) See § 38 of the 1915 Act on contract (Lagen om avtal och andra rättshandlingar på förmögenhetsrättens område, SFS 1915:218).

the provisions, must not be unreasonable. The same is the case with respect to non-competition provisions.

3 Winding up the investment in employment relationships

Restrictions concerning the company’s possibilities to terminate employment relationships provide a risk for the company. If the market situation changes or if the work that an employee performs is no longer needed or profitable for the company, it can be vital for the company to quickly terminate employment relationships. Labour-costs are often a major part of the company’s total costs.

In Sweden the employer must have a valid reason to terminate an open-ended employment contract and he must, in those cases relevant here, observe a period of notice. The valid reasons for terminating an open-ended employment contract can be divided into two categories, which follow different rules: i) dismissal for reasons related to an individual employee and ii) dismissal for economic or other reasons not related to an individual employee.

The fact that an individual employment contract is not profitable but gives rise to a loss for the company is probably not in itself a valid reason for terminating that employment contract (for reasons related to an individual employee), at least not if the employer is a bigger company. A reduction in performance due to old age or sickness, including alcoholism and mental illness, is for example normally not a valid reason for terminating the

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16 According to the legislation the length of the period of notice vary between one and six months, mainly depending on the employee’s age, see § 11 of the Employment Protection Act. Collective or individual agreements can prescribe a longer period of notice.

17 See regarding ILO the 1982 Termination of Employment Convention (no. 158) and the Recommendation (no. 166) on the same subject.

18 This case is classified as a dismissal for reasons related to an individual employee, although the reasons are of a purely economic nature, see AD 1994 nr 122.

19 See Kent Källström "Alkoholpolitik och arbetsrätt – En komparativ studie av missbruukes anställningsskydd" [1993].
employment contract; the employment contract may be terminated not until it is entirely clear that the employee is permanently unable to perform work of any importance for the employer.\textsuperscript{20} There are, however, a couple of examples from case law where the courts have taken into consideration in the overall assessment the fact that the employment contract gives rise to a loss for the company in order to determine whether there is a valid reason for termination or not.\textsuperscript{21} – The validity of a dismissal for reasons related to an individual employee can be contested in a court of law by the employee (or his organisation). In such a case the employment relationship is in full force until the question of validity is finally settled by the court or otherwise.

Termination of the employment contract for economic or other reasons not related to an individual employee is in Sweden called dismissal for shortage of work. The main rule here is that it is the employer’s prerogative to decide if there is a shortage of work, i.e. a redundancy situation. The employer’s decision to reduce the work-force can, as a rule, not be contested in a court of law. But before the employer is allowed to make that decision he must, at his own initiative, take up – and bring to an end – joint-regulation negotiations with the local trade unions at the workplace. There is no time limit for the duration of the negotiations, and if the trade union so requests the employer is obliged to negotiate a second time with the central (national) trade union before he is allowed to decide on collective redundancies. The employer must also in advance notify the Regional Labour Market Board of projected redundancies.\textsuperscript{22}

The employer is hence free to decide – after negotiations – if he should resort to collective dismissals, but he is, when he decides on collective dismissals, not free to choose whom to dismiss and whom to keep of his staff. According to the legislation a strict seniority-rule is as a matter of principle applied; the employer must retain the employees with the longest period of service and he is not allowed to choose the most effective or profitable employees. The employer’s interest in having access to a competitive work-

\textsuperscript{20} See the Bill 1973:129 p. 126 f.
\textsuperscript{21} See AD 1978 nr 13 and 161 and compare AD 1994 nr 122.
force after the reduction is respected only by a rule to the effect that the remaining employees must have “sufficient qualifications” for the work to be carried out after the reduction, but this normally means only that the employees must be able to learn to perform the work adequately within a reasonable period of time. – The rules on the selection of the employees to be made redundant can be overridden by a collective agreement, which means that the employer – or an organisation of employers – and a competent trade union can through collective agreement decide on other selective criteria or solely decide which employees are to be dismissed in a particular redundancy-situation. Such a collective agreement is often concluded in connection with the joint-regulation negotiations preceding the decision on collective dismissals.

What has been said so far indicates that the company has limited possibilities to quickly terminate open-ended employment contracts that are not profitable for the company and that the entry into such an employment contract therefore constitutes a certain economic risk for the company that is difficult to calculate on beforehand. One way of reducing the risk is to test the worker before entering into an open-ended employment contract. Many measures aimed at promoting employment in the field of state labour market policies provide possibilities for the company to test workers, often at a low initial cost for the company. Temporary employment contracts (of a fixed duration) can, in those cases such employment contracts are allowed, also provide a way for the company to find out the qualification of the workers.\(^\text{23}\) According to the Swedish legislation an employment contract can be concluded for a trial period not exceeding six months.\(^\text{24}\)

Another way for the company of handling the risk that is involved with open-ended employment contracts is not to use such employment contracts and instead seek other ways of getting the job done. Temporary employment contracts can, when they are allowed, be used. Another possibility is to contract out specific tasks to a subcontractor.\(^\text{25}\) The company can also

\(^{23}\) In Spain one of the valid grounds for a temporary employment contract has been to promote employment. Also in Sweden the possibilities to use temporary employment contracts was extended during 1994 in order to promote employment.

\(^{24}\) § 6 of the Employment Protection Act.

\(^{25}\) The EC-directive 77/187 on the approximation of the laws of the Member States relating to the safeguarding of employees’ rights in the event of transfer of undertakings, businesses or parts of businesses must be observed here, see for example cases
hire personnel from another company.\textsuperscript{26} \textsuperscript{27} A recent organisational trend seems to have been for companies to concentrate on their core activities and buy peripheral services needed from companies specialised on those services. Furthermore, some labour market policy state programmes can in reality provide a possibility for the company to use labour without entering into an employment contract with full employment protection.

From what has been said follows that there are several restrictions regarding the termination of open-ended employment relationships which pose a risk for the company. If it is difficult and expensive for the company to terminate open-ended employment relationships, the possibilities to change the contents of those employment relationships can be of importance for the company in order to manage the risk that is involved.

4 Changing the contents of the employment relationship

If the company has economic difficulties, reducing the wages or increasing the working-hours (but not the salary) can be an alternative to the termination of employment relationships. In Sweden the employer is not obliged to consider such measurements before resorting to collective dismissals. And in most cases collective agreements prevent the employer from bringing about such changes even if he gets consent from the employees concerned. But sometimes the employer can withdraw some additional benefits that are not protected by collective agreement.\textsuperscript{28} There seems in practice to be

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The trade union has, subject to certain conditions, a right to veto the employer’s contemplated decision to use non-employed labour for his activities, see §§ 38–40 of the 1976 Act on Joint Regulation of Working Life (Lagen om medbestämmande i arbetslivet, SFS 1976:580).

See for example AD 1992 nr 27 and 1993 nr 61; if the benefit – or the salary, see AD 1994 nr 122 – is not protected by collective agreement but constitutes a part of the individual employment contract, the employer has technically to terminate the contract and offer a new contract without the benefit.
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limited possibilities for the company to unilaterally influence the cost per hour for employees with open-ended employment contracts.

Normally the company has greater opportunities to unilaterally change other aspects of the employment relationship. One of the characteristics of the employment relationship is that the employee is subordinate to the employer. The main principle is that it is up to the employer to unilaterally decide what work is to be performed where, how and when. The right for the employer can be limited by provisions in the individual employment contract regarding, for example, where work is to be performed. Restrictions can also be laid down by collective agreements. The employee is not obliged to perform work that falls outside the scope of the relevant collective agreement. But the scope of a collective agreement is normally very wide and encompasses all tasks for the employer that are naturally connected with the tasks that the agreement primarily is aimed at regulating, provided that the employee has the occupational skills to perform the task. Legislation regarding, for example, working time and working environment provides the scope for the employer’s right to unilaterally decide on the content of the employment relationship. Also principles developed through case law can restrict the employer’s right.

In disputes regarding the extent of an employee’s contractual obligation to work the employee’s trade union has what is called a priority of interpretation. Before the court decides on the dispute the employee is, temporarily, relieved from his obligation to obey the employer if he instead follows the interpretation advocated by his trade union. This means that the employer normally cannot get the disputed work done without going to court.

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29 A white-collar worker is often regarded to have a certain position according to the employment contract, and he is then, as a main rule, not obliged to perform tasks that are not in accordance with that position.

30 An example here is the collective agreement for the municipal sector prescribing that the employer must have “manifest reasons” to transfer an employee.

31 See, for example, AD 1929 nr 29. This principle applies to collective agreements for white-collar workers as well, see AD 1995 nr 31.

32 The employer must according to case law have a valid reason to permanently transfer an employee for reasons related to the individual employee, if the transfer has far-reaching consequences for the employee, see for example AD 1978 nr 89.

33 The rule on the trade union’s priority of interpretation is laid down by § 34 of the Act on the Joint Regulation of Working Life.
The employer’s execution of his right to unilaterally decide on the working conditions is, furthermore, generally restricted by legislation and collective agreements on joint regulation, i.e. the right for trade unions to influence the employer’s decision-making process. An employer, who is (or at least usually is) bound by a collective agreement, must at his own initiative take up and bring to an end joint regulation negotiations with the local trade union at the workplace before he is allowed to decide on a more important change of his activities or of the working or employment conditions for a union member. The joint regulation procedure can make it difficult for the company to take necessary and speedy decisions. But it can on the other hand also bring about a better acceptance and understanding among the employees for the decisions and changes and thereby promote necessary changes. A recent survey in Sweden shows that joint regulation in general is accepted and appreciated by the companies and the shop stewards as well.\(^{34}\)

\(^{34}\) See Sören Wibe "*Medbestämmandelagen och samhällsekonomin*", appendix 1 to the report *Arbetsrättsliga utredningar*, SOU 1994:141.