

## LEGAL UPDATE LABOUR AND EMPLOYMENT LAW

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# Cologne Regional Labour Court: Damages due to delayed setting of performance target for company-related objectives

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Employment contracts often contain provisions on variable remuneration. If the employer had promised the employee variable performance-related remuneration upon achieving certain objectives, a distinction needs to be made between **performance agreements** on the one hand, and **performance targets** on the other. In performance agreements, the objectives are mutually determined by the parties to the employment contract. Conversely, performance targets are only set by the employer. Determining whether something is a performance agreement or a performance target comes down to the interpretation of what was agreed in the contract.

The Federal Labour Court (Bundesarbeitsgericht, BAG) held in two decisions dated 12 December 2007 (10 AZR 97/07) and 17 December 2020 (8 AZR 149/20) that the employer's culpable breach of their obligation to mutually agree on objectives for a target period with the employee entitles the employee to assert a claim for damages at the end of the target period, stating that the employee should in principle be treated as if they had actually achieved 100% of the objectives. The BAG held that a performance *agreement* can only fulfil its incentive function if the employee is already aware of

the objective to be achieved when doing their job and knows which personal and/or company-related objectives the employer places value on achieving. It is not possible to set targets that fulfil the intent and purpose of a performance agreement for a period in the past. At the expiry of the target period, i.e. generally at the expiry of a calendar year or financial year, an employee can therefore demand damages if no performance agreement had been set.

The BAG left open the question of (1) what applies when an employer is "only" obligated to set a (unilateral) performance target and this is not set during the target period and (2) whether a (full) claim for damages can arise even before the target period has finished.

The Cologne Regional Labour Court (Landesarbeitsgericht, LAG) dealt with both of these questions in its recent judgment dated 6 February 2024 (4 Sa 390/23) and the appeal to the BAG was expressly permitted due to these legal questions having not yet been answered at the highest level of the judiciary.

## Facts of the matter

The case upon which the decision is based involved an employment contract of an employee with variable remuneration in the amount of EUR 30,637.00 gross if their objective was 100% achieved, where the respective objectives were to be defined by their supervisor at the beginning of each calendar year. Therefore, a performance target had been agreed. A Works Agreement that was agreed later stated that each employee would receive a performance target by 1 March which was to be comprised up to 70% of company objectives and up to 30% of individual objectives. Specific information regarding the company objectives for the 2019 calendar year was only available, however, in mid October 2019. The employee subsequently filed a claim for damages for the full amount of variable remuneration, including in relation to the company-related objectives, as these were defined too late in the financial year by the employer and therefore must be paid as if the objectives had been reached in full. Therefore, following the case law of the BAG, a corresponding right to claim for damages accordingly arises in relation to the lack of agreed performance agreements.

The employee's claim was initially rejected at first instance by the ArbG. The court held that the company objectives, although received in Autumn 2019, were still defined by the employer within the 2019 financial year. As the target period had not yet concluded, it was still possible to determine the company objectives and therefore were still able to be used. It was argued that delayed and incomplete missing performance targets could give rise to a right to file a claim for damages as well; this, however, did not apply to company-related objectives, but only for individual objectives. The court held that there was therefore no right to claim damages in relation to company-related objectives as a result of delayed performance targets.

The employee successfully appealed against this ruling, claiming that the company objectives for 2019 were delayed by the employer, meaning it was the case that the company-related objectives were 100% achieved. The employee argued that the differentiation by the ArbG between individual objectives on the one hand and company-related objectives on the other was inappropriate. Therefore, a claim for damages on account of delayed performance targets (for the company-related objectives) should be made for the full amount.

## Decision of the Cologne Regional Labour Court

The Cologne LAG followed the reasoning of the employee, granted the appeal in full and ordered the employer to pay damages for the performance targets (for the company-related objectives) not being determined on time for the 2019 fiscal year.

The Cologne LAG first clarified that a missing performance target should be treated in the same way as a missing performance agreement. It stated that a missing performance target can give rise to an employee's right to claim for damages in the same way. Furthermore, the Cologne LAG made it expressly clear that a delayed performance target within the current financial year should be treated exactly the same as a (completely) missing performance target. If a performance target is only set at a later point during the relevant financial year, such that it cannot meaningfully fulfil its incentive function, it should be treated as if it had not been set at all. Such delay should be assumed to have taken place if more than three quarters of the financial year has already elapsed. This does not just apply to individual (personal) objectives, but also to company-related objectives, as the incentive function is not necessarily ruled out

just because the missing performance target relates to company objectives.

## Comments

The decision of the Cologne LAG is remarkable in two ways. On the one hand, it was expressly clarified that an employee's right to claim damages does not only arise in relation to completely missing performance targets, but also arises in relation to delayed performance targets (for the full amount). On the other hand, the Cologne LAG also made it expressly clear that this does not just apply to individual objectives but also to company-related objectives.

Even if the judgment of the Cologne LAG is not yet final and a decision of the BAG is still to be awaited, employers would already be well advised to observe the requirements resulting from the decision. Employers should therefore

set employees' performance targets not just as early as possible in the current financial year and document this in writing, but should also from the outset extend this to both individual and company-related objectives, provided achieving the objective associated with the variable remuneration covers both individual as well as company-related objectives. Otherwise there is a danger that nevertheless 100% of the variable remuneration must be paid to the employee as damages (through the back door as it were), as the case law generally assumes that 100% of the objective have been achieved. In theory, it is possible that an employer could present evidence that the objectives have not been met, but in practice this is quite difficult. Employers should therefore always define clear (and achievable) objectives at an early stage to avoid such disputes and document this in writing in a demonstrable way to the employee.

### Note

This overview is solely intended for general information purposes and may not replace legal advice on individual cases. Please contact the respective person in charge with GÖRG or respectively the author Timo Rehfish on +4922133660541 or by email to [trehfish@goerg.de](mailto:trehfish@goerg.de) an. For further information about the author visit our website [www.goerg.com](http://www.goerg.com).

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