THE CONSTITUTIONAL COURT
OF THE REPUBLIC OF LATVIA

J U D G E M E N T

On Behalf of the Republic of Latvia

Riga, 10 June 2011

Case No. 2010-69-01

The Constitutional Court of the Republic of Latvia composed of the Chairman of the Court session Gunārs Kūtris, and justices Kaspars Balodis, Aija Branta, Kristīne Krūma, Vineta Muižniece and Viktors Skudra

having regard to a constitutional complaint submitted by: Einārs Matjušenoks, Vjačeslavs Aleksejevs, Ilga Apša, Dace Artemjeva, Rita Aumeistare, Aivars Balodis, Tatjana Bļašona, Daina Čaune, Anželika Dinaburgska, Vladimirs Dmitrijevs, Jānis Elsis, Mārīte Grāpe, Bruno Ģīmis, Ilzīte Ignate, Modris Jēkabsons, Ieva Kalniņa-Kūla, Artūrs Keišs, Gunta Kļimoviča, Alda Kozlova, Ineta Kraglika, Juris Kukainis, Lauris Kukainis, Ludmila Kurjanoviča, Diāna Leoke, Biruta Ločmele, Iveta Lopatko, Gatis Lovkins, Inese Mackēviča, Madars Maske, Svetlana Meļķe, Janīna Mēnese, Rudīte Mince, Evita Ozola, Vita Ozola, Inese Ozola, Benita Pommere, Dainis Priedītis, Ilze Pužule, Ilona Rulle, Marija Savenkova, Māra Sekača, Anita Šalna, Ieva Šalna, Ģirts Šnēvels, Talivaldis

Tomsons, Sandra Treimane, Ilona Ubeiko, Gunita Ūdre, Mikus Ulmanis, Jeļena Vaivode, Igors Vanags, Gints Vilks, Romāns Zadorožnijs, Sandija Zaļupe, Zita Zandere, Solvita Zvirbule, Modris Zvirbulis, Siguta Vītola and Aldis Dudelis (hereinafter all together referred to as – Applicants),

according to Article 85 of the Satversme (Constitution) of the Republic of Latvia and Article 16 (1), Article 17 (1) Indent 11, and Article19.^{2} and Article 28.^{1} of the Constitutional Court Law,

on 20 May 2011, in writing examined the case

„On Compliance of Para 6 and Para 7 of Transitional Provisions of the Law "On Protection of Employees in Case of Insolvency of Employer" with Article 1 and Article 91 of the Satversme".

The Facts

1. On 20 December 2001, the Saeima [Parliament] of the Republic of Latvia adopted the Law "On Protection of Employees in Case of Insolvency of Employer" (hereinafter – the Employees Protection Law). The Employees Protection Law regulates general provisions regarding satisfaction of claims of employees in case of insolvency of an employer and the procedure for collection and use of means of the employee claim guarantee fund (hereinafter – Guarantee Fund).

1.1. Section 2 (1) of the Employees Protection Law provides that within the meaning of this Law, insolvency of an employer shall be in effect from the day when a court judgment regarding insolvency of the employer or a credit institution enters into legal effect.

1.2. In the wording that was effective as from 1 January 2007, Section 5 (1) of the Employees Protection Law provided:

Employee claims shall be satisfied from the resources of the employee claim guarantee fund in the following amounts:

1) work remuneration for the last three months of employment legal relationship in twelve months before the insolvency of the employer came into effect;

2) reimbursement for annual paid leave the right to which has been acquired in the twelve months before the insolvency of the employer came into effect;

3) reimbursement for other types of paid leave in last three months of employment legal relationship in the last twelve months before the insolvency of employer came into effect;

4) severance pay in the minimal amount prescribed by law;

5) reimbursement for damages for the whole unpaid time period;

6) reimbursement for damages for the four subsequent years."

1.3. On 18 June 2009, the Saeima adopted the Law "Amendments to the Law "On Protection of Employees in Case of Insolvency of Employer"" (hereinafter – Amendments) that came into force on 10 June 2009.

The Amendments supplemented Section 5 (1) indent 4 of the Employees Protection Law by the following words and a figure "the right to which has been granted no earlier than in the last twelve months before the insolvency of employer came into effect", whilst Transitional Provisions of the Employees Protection Law has been supplemented with Para 6 and Para 7 in the following wording:

„6. To satisfy claims of those employees whose applications have been submitted to the Insolvency Administration in the period from 10 July 2009 to 31 December 2011, Provisions established in Section 5 (1) indent 1, 2, 3 and 4 and Section $5.^1$ of the present Law, the following regulatory framework shall be applied – claims of employees shall be satisfied from the resources of the employee claim guarantee fund at the following amounts:

1) work remuneration for the last three months of employment legal relationship in twelve months before the insolvency of the employer came into effect if it is calculated pursuant to requirements of normative acts and monthly earning do not reach the minimum wage established in the State as on the date of coming into effect of insolvency;
2) reimbursement for annual paid leave the right to which has been acquired in the twelve months before the insolvency of the employer came into effect if it is calculated pursuant to requirements of normative acts and monthly earning do not reach the minimum wage established in the State as on the date of coming into effect of insolvency;
3) reimbursement for other types of paid leave in last three months of employment legal relationship in the last twelve months before the insolvency of employer came into effect if it is calculated pursuant to requirements of normative acts and monthly earning do not reach the minimum wage established in the State as on the date of coming into effect of insolvency;
4) severance pay in the minimal amount prescribed by law, the right to which has been granted no earlier than in the last twelve months before the insolvency of employer came into effect, if it is calculated pursuant to requirements of normative acts and monthly earning do not reach the minimum wage established in the State as on the date of coming into effect of insolvency.

7. The sum of employee claims to be satisfied mentioned in Section 5 (1) indent 1, 2, 3 and 4 and Section 5.[1] of the present Law, of social insurance obligatory employee payments related thereto and of the personal income tax does not exceed four minimum wages established in the State as on the date of coming into effect of insolvency if employees' application for satisfying their claim has been submitted to the Insolvency Agency in the period from 10 July 2009 to 31 December 2011."

2. The Applicants ask the Constitutional Court to recognize Para 6 and Para7 of Transitional Provisions of the Employees Protection Law (hereinafter – Contested Norms) as non-compliant with Article 1 and Article 91 of the Satversme of the Republic of Latvia (hereinafter – the Satversme).

It has been indicated in the application that the company where the Applicants have worked, was recognized as insolvent on 2 June 2009. On 12 June 2009, the Applicants received employer's notice of default. All submitted and recognized claims of the employees were submitted to the Insolvency Administration on 9 November 2009. Since the company did not have necessary means to cover the claim of the employees, the State agency "*Maksātnespējas administrācija*" ["Insolvency Administration"] (hereinafter – Insolvency Administration) decided satisfying the claims of the employees from the resources of the Guarantee Fund.

The Contested Norms establish the amount, at which employees' claims are covered from the resources of the Guarantee Fund, the claims having been submitted to the Insolvency Administration in the period from 10 July 2009 to 31 December 2011. This amount is less than the one established in Section 5 of the Employees Protection Law.

2.1. The Applicants hold that the Contested Norms fail to comply with the principle of legitimate expectations enshrined in Article 1 of the Satversme establishing that in case of unfavourable amendments, a person should be provided a lenient transition to the new regulatory framework. The Applicants could legally trust into the fact that they would be disbursed compensation from the Guarantee Fund at the amount established in Section 5 of the Employees Protection Law. Consequently, as the legislator reduced the amount of disbursement from the Guarantee Fund, it had the duty to establish a lenient transition to the new regulatory framework. Namely, when adopting the Contested Norms, the legislator did not have the right to apply them to employees, whose employer's insolvency came into effect before coming into force of the Contested Norms.

The Applicants emphasize that legitimate trust into receipt of stipulated means in case of insolvency of the employer not been granted to them earlier than on the date when an insolvency procedure administrator (hereinafter – administrator) submitted employees' claims to the Insolvency Administration as it is indicated by the Saeima or on the date of coming into effect of insolvency of a company. Namely, it took place after coming into force of the Employees Protection Law. When working in a company, the Applicants trusted into the fact that, in case of insolvency of the employer, they would not be deprived of means of subsistence since they would receive undisbursed wage and other payments from the Guarantee Fund. This legitimate trust (rather than hope, as it is indicated in the Saeima reply) has formed based on the Employees Protection Law.

2.2. According to the Applicants, the Contested Norms neither comply with the principle of equality enshrined in Article 91 of the Satversme. Both, the Applicants and employees whose claims have been satisfied before coming into force of the Contested Norms, enjoy equal and comparable conditions. However, the legislator has restricted the amount of disbursements from the Guarantee Fund by thus establishing unequal attitude without reason.

The Applicants also indicate that the legitimate aim, namely, satisfaction of claims of all employees at full amount, could be reached by selecting a more lenient measure. One of such alternative measures could be increase of the share of the State entrepreneurial risk fee and establishing at the level of 2003, 2004 or 2005. Changes in the share of the State entrepreneurial risk fee require spending no means from the State budget. Increase of payments to be made by an employer would be proportional because, first, the State entrepreneurial risk fee has been considerably reduced from 2003 to 2009 and, second, the State entrepreneurial risk fee for an employer having several hundreds of employees would not be high. If the State entrepreneurial risk fee would constitute 45 santimes per months per one employee (which is less than in 2003 and the same as in 2005), then the State would collect 1 792 596 lats per year, whilst with the State

entrepreneurial risk fee at the amount of 75 santimes per month per one employee would constitute 4 481 490 lats per year.

The Applicants hold that the action of the legislator is not proportional because it is not compliant, namely, benefit gained by the society is not greater than detriment caused to the rights of a person. Although under economic recession circumstances funding can be reduced, it is still necessary to observe constitutional principles, including that of solidarity.

3. The institution that issued the contested act, the Saeima holds that the Contested Norms do comply with norms of a higher legal force and therefore ask the constitutional Court to recognize them as compliant with Article 1 and Article 91 of the Satversme.

The Saeima indicates that, in a certain period, the Contested Norms establish restrictions in respect to satisfying employees' claims to the Guarantee Fund.

3.1. Initiation of insolvency procedure does not give the right to immediate disbursement of compensation from the Guarantee Fund because, first of all, employees' claims would be assessed by the administrator. Moreover, it is possible to satisfy only such claims that have been recognized by the administrator and included into the register of creditors' claims. Consequently, the Saeima holds that the Applicants were granted legitimate trust into satisfying of their claims as from 6 November 2009 only. However, the right to satisfaction of claims could have been granted only after the Insolvency Administration adopts respective decision. Moreover, the point of reference established in the Contested Norms, namely, application of the administration, does comply with the principle established in Section 10 of the Employees Protection Law.

The Contested Norms assure the possibility to satisfy claims of all persons at a limited extent provided that these persons have the right to receive compensation from the Guarantee Fund in case of insolvency of employer, as established in normative acts.

The Saeima indicates that the amount of the Guarantee Fund is not constant and it may change. As incomes of the State entrepreneurial risk fee changes and number of insolvency processes increase, the amount of means at the disposal of the Guarantee Fund may reduce considerably. Consequently, the possibility of the State to satisfy claims of employees of insolvent employers from the resources of the Guarantee Fund depends on incomes into the Fund.

In 2009, as economic crisis continued, the amount of means at the disposal of the Guarantee Fund became by 20 per cent less than planned. To cover claims of employees, the Guarantee Fund received additional funding based on the surplus of previous years of the Fund was granted. However, it was also necessary to take immediate measures to assure satisfaction of claims of all employees. Therefore the right to satisfying a claim from the resources of the Guarantee Fund in case of insolvency of an employer are restricted with reasonable grounds; moreover, the restriction has been established for the period up to 31 December 2011.

The Contested Norms do not mean that the State has refused fulfilling any duty; they only establish a terminated restriction in respect to disbursements. Thus the State can, in the long term, ensure stability in respect to satisfaction of employees' claims within the frameworks of resources available, which determines the legitimate aim of the Contested Norms, namely, protection of rights of other persons and assurance of welfare of the society.

The Saeima emphasizes that an employee who has not received his or her wage because of the employer's insolvency can start new legal labour relations. Moreover, he has the right to State guaranteed social benefits in the frameworks of the social insurance system disregarding of the fact whether the insolvent employer has or has not made. Consequently, the social insurance system and the right to claim established in Section 137 (4) of the Insolvency Law shall be regarded as a compensating mechanism.

The Contested Norms do comply with the principle of proportionality and therefore with that of legitimate expectations because protection of rights of other persons and of social welfare is constitutional values that are protected by redistributing common benefit and balancing state budget income and expenses.

3.2. When assessing compliance of the Contested Norms with Article 91 of the Satversme, the Saeima indicates that establishment of a new regulatory framework or a transitory one always causes another attitude if compared to the one existing before; however, there is no reason to regard it as a different attitude. The Applicants do not enjoy comparable circumstances if compared to person who have already been disbursed compensation from the Guarantee Fund.

4. The summoned person, the Cabinet of Ministers indicates that each employer annually pays the State entrepreneurial risk fee to cover expenses of covering employees' claims from the resources of the Guarantee Fund.

Expenses from the Guarantee Fund established in the Employees Protection Law are regarded as social guarantee for employment period of an employee in case if the employer is no more able fulfilling its liabilities in case of insolvency thereof.

Economic recession has had a considerable impact on the national economy. As the economic situation deteriorated, the collected amount of State entrepreneurial risk fee has reduced by 20 per cent if compared to the estimated amount, whilst the number of claims to be satisfied has increased. In 2009, it was planned to satisfy 1087 employees' claims from the resources of the Guarantee Fund, though in fact 2015 employees' claims were satisfied, which is by 47 per cent more. Therefore, when assessing proportionality of the Contested Norms, one cannot ignore economic factors.

The Contested Norms establish a small and terminated reduction in amount of means to be disbursed form the Guarantee Fund. Therefore the Contested Norms shall be

regarded as a socially responsible solution because legal interests of certain persons are co-ordinated with those of the entire society.

5. The summoned person, the Insolvency Agency holds that the opinion of the applicant is ungrounded. In 2009, the Guarantee Fund had 1 215 000 lats at its disposal to satisfy claims of employees in case on insolvency of the employer; however, the Insolvency Agency prognosticated that 4 213 413 lats would be needed to satisfy all employees' claims. Consequently, if there were no restrictions to disbursements from the Guarantee Fund, the State would not be able to satisfy claims of all those persons who have the right to receive compensation in case of insolvency of the employer pursuant to normative acts. Therefore such restriction has been imposed on disbursements from the Guarantee Fund that permits continue assuring protection of employees in case of insolvency of employers under certain economic circumstances.

The right of employees to receive means from the Guarantee Fund in case of insolvency of the employer is not denied as such, it is only restricted for a certain time period in a reasonable way.

The right of an employee to wage follows from his or her legal labour relations, whilst guaranteeing of the wage is a duty of the employer. In case if the employer becomes insolvent and is no more able to fulfil its liabilities, then the employee shall have the subjective right to receive means from the Guarantee Fund. Therefore disbursements from the Guarantee Fund cannot be regarded as social benefits.

Pursuant to Directive 2008/94/EC of the European Parliament and of the Council of 22 October 2009 on protection of employees in the event of the insolvency of their employer (hereinafter – Directive 2008/94/EC), each member state shall ensure only the minimum protection, and they have the right to restrict disbursements envisaged in the Directive. Consequently, Member States of the European Union have the right to

establish restrictions to disbursements from the Guarantee Fund taking into account economic situation of the state.

6. The summoned person, the Ombudsman of the Republic of Latvia (hereinafter – Ombudsman) indicates that the Contested Norms distinguish between two groups of persons who can exercise their right to satisfaction of a claim from the resources of the Guarantee Fund and they are: persons whose claims have been submitted to the Insolvency Agency before 9 July 2009 and persons whose claims have been submitted to the Insolvency Administration after the above mentioned date. Persons pertaining to the both above mentioned groups have the right to apply for satisfaction of claims from the resources of the Guarantee Fund. Consequently, both groups of persons enjoy equal and comparable conditions.

Legitimate aim of the Contested Norms is balancing of incomes and expenses of the Guarantee Fund because they are considerably influenced by the economic situation and the rapid increase of unemployment in the State. Taking into account the self-funding principle of the Guarantee Fund, restriction of respective disbursements shall be regarded as an appropriate solution, by means of which the legislator can assure reaching of the legitimate aim.

When assessing whether it was possible to reach the legitimate aim by applying other measures that would restrict the rights of a person at a lesser extent, the Ombudsman indicates that selection of necessary measures for reaching of the legitimate aim falls within the field of competence of the legislator. Therefore, here it is necessary to assess only the fact whether the measure selected by the legislator restricts the fundamental rights in a non-proportional manner.

Taking into account the fact that means of the Guarantee Fund are used only for satisfying employees' claims in case of insolvency of the employer, as well as the fact that in 2009 the State has performed considerable reforms to reduce expenses of the State

budget not only in respect to protection of employees in case of insolvency of the employer but also in other fields, the Ombudsman has no doubt that respective action by the legislator was indispensable.

According to the Ombudsman, the Contested Norms assure that the benefit gained by the society is greater than the detriment caused to the rights of a person. In fact, the legislator has not refused satisfying employees' claims in case of insolvency of the employee; it has only restricted the amount of compensation during the transition process. This is permitted with Article 13 of the Convention No. 173 concerning the protection of workers' claims in the event of the insolvency of their employer and Article 4 of the Directive 2008/94/EC. Likewise, one should also take into account the fact that, in case of unemployment, these persons have the right to social unemployment benefit.

Consequently, the Contested Norms do not contradict the principle of equality included in the first sentence of Article 91 of the Satversme.

The Ombudsman agrees with what has been indicated in the Saeima reply, namely, that initiation of insolvency procedure as such does not give immediate right to receive compensation from the Guarantee Fund. Therefore the opinion of the Applicants that the Contested Norms infringe the principle of legitimate expectations is ungrounded. Persons could have trusted into the fact that the State would protect employees in case of insolvency of the employer; however, they could not legally trust into a compensation of a certain amount because claims of these persons had not yet been assessed and no decisions regarding satisfaction of them have been adopted. Moreover, it is necessary to take into account the field of right, to which the protected rights pertain. Exercise of social rights that also include protection of employees depends on available resources; therefore, in this respect, persons cannot be protected against changes in normative regulatory framework.

Consequently, the Contested Norms do not contradict the principle of legitimate expectations and that of equality.

7. The summoned person, the Free Trade Union Confederation of Latvia [*Latvijas Brīvo arodbiedrību savienība*] (hereinafter – the LBAS) holds that the Applicants, as well as employees who have lost their work in case of insolvency of the employer but whose claims have been submitted to the Insolvency Administration before 10 July 2009 enjoy equal conditions. Consequently, the Contested Norms restricts the rights of the applicants, though the restriction has a legitimate aim, i.e. to assure satisfaction of all employees' claims at least at a reduced amount.

According to the LBAS, the restriction established to the right of employees is not proportional with the benefit gained by the society in general from the restriction. The only possibility of employees to receive their wage in case of insolvency of the employer is to request it from the Guarantee Fund. The information gathered by the Ministry of Justice shows that other solutions for receiving the above mentioned remuneration are non-effective.

By referring to the letter of the Ministry of Justice prepared when drafting the Amendments, the LBAS indicates that, since 2006, incomes from payment of the State entrepreneurial risk fee have not been transferred to the Guarantee Fund. According to the LBAS, an alternative solution is to deal with the issue regarding forming funds of the Guarantee Fund rather than to adopt the Contested Norms and reduce expenses of the Guarantee Fund.

By referring to the opinion of the Saeima Legal Office on the draft Amendments, the LBAS indicates that the regulatory framework is not the most lenient solution for assuring long-term social stability by satisfying employees' claims at the amount of resources available.

Consequently, the LBAS holds that the Contested Norms do not comply with the principle of legitimate expectations because "the established infringement of legitimate expectations is unjustifiable".

8. The summoned person, the Employers' Confederation of Latvia [*Latvijas Darba devēju konfederācija*] indicates that the restrictions established in the Employees Protection Law have objective and reasonable grounds taking into account circumstances of economic recession.

The Contested Norms do not impact too many persons and assures an appropriate balance between interests of the society and those of certain persons.

The Findings

9. The Applicants hold that the Contested Norms establish an ungrounded different attitude towards those employees of insolvent employers who submitted their applications to satisfy a claim to the Insolvency Administration before 9 July 2009 and those who have submitted their applications after 10 July 2009. Consequently, the contested regulatory framework does infringe Article 91 of the Satversme.

Article 91 of the Satversme provides: ".All human beings in Latvia shall be equal before the law and the courts. Human rights shall be realized without discrimination of any kind. " Objections of the Applicants are related to the principle of equality enshrined in the first sentence of Article 91 of the Satversme; consequently, the Contested Norms shall be assessed in the context of the principle of equality.

10. When interpreting the first sentence of Article 91 of the Satversme, the Constitutional Court has recognized that the principle of forbids the state institutions to pass norms, which without a reasonable ground permits different attitude to persons who are in really equal and comparable conditions. The principle of equality allows and even demands different attitude to persons who are in different circumstances, as well as

allows different attitude to persons who are in equal circumstances, if there is an objective and reasonable ground (*see: Judgment of 5 December 2001 by the Constitutional Court in the case No. 2001-07-0103, Para 3 of the Findings*). A differentiated attitude is discriminating, if it does not have an objective and well-grounded reason, i.e. – a legitimate aim or if the chosen means and the advanced objectives are not proportionate (*see: Judgment of 23 December 2002 by the Constitutional Court in the case No. 2002-15-01, Para 3 of the Findings*).

When assessing whether the Contested Norm complies with the first sentence of Article 91 of the Satversme, the Constitutional Court has to investigate the following: 1) whether and what persons (groups of person) enjoy equal and, according to certain criteria, comparable conditions; 2) whether the Contested Norm provides for a different attitude towards these persons; 3) whether this attitude has an objective and reasonable grounds, namely, whether the principle of proportionality has been observed (*see: Judgment of 18 February 2011 by the Constitutional Court in the case No. 2010-29-01, Para 12*).

11. The right to satisfying of claims from the resources of the Guarantee Funds pursuant to Section 3 of the Employees Protection Law is granted to person who have been or are in an employment legal relationship with an employer, who has been declared insolvent, if the referred to claims have been included in creditor's meeting approved recognized unsecured creditor claims list.

In fact, the legislator has not changed the employees' protection system in case of insolvency of the employer and the group of persons who have the right to satisfying of the claim from the resources of the Guarantee Fund; it has only limited amount of disbursements from the Guarantee Fund for the period from 10 July 2009 to 31 December 2011. Consequently, the Contested Regulatory Framework no doubt determines two groups of persons having the right to satisfying of the claim from the resources of the Guarantee Fund:

1) persons whose claims have been submitted to the Insolvency Agency before 9 July 2009;
2) persons whose claims have been submitted to the Insolvency Agency after 9 July 2009;

Both of the above mentioned groups include persons that have the necessary prerequisites to apply for satisfying of their claim from the resources of the Guarantee Fund.

Consequently, both groups of persons enjoy equal and comparable conditions.

12. When adopting the Contested Norms, the legislator has restricted the amount of disbursements from the Guarantee Fund. By means of the Contested Norms, in the period from 10 July 2009 to 31 December 2011, certain restrictions have been established in Section 5 (1), (2), (3) and (4), as well as Section $5.^{1}$ (2) of the Employees Protection Law in respect to disbursements from the Guarantee Fund. Therefore, after coming into force of the Contested Norms, the above mentioned expenses were bound to the minimum wage established in the state as on the date of declaring of the employee insolvent by also determining that a disbursement shall not exceed four minimum wages.

Consequently, the Contested Norms assure that the both groups of persons have the right to receive disbursement from the Guarantee Fund; however, they establish a different attitude towards them in respect to the amount of such disbursement.

13. Article 116 of the Satversme does not refer to the rights guaranteed in Article 91 of the Satversme, however this does not mean that these rights are absolute and they cannot be restricted. The Satversme is a single whole, and norms included therein shall be interpreted systematically. The assumption that the rights established in

Article 91 of the Satversme cannot be restricted would contradict its aims and fundamental rights of other persons established in other articles of the Satversme.

The Constitutional Court has already concluded that "equality allows a differentiated approach, if it can be justified in a democratic society" (*see: Judgment of 26 June 2001 by the Constitutional Court in the case No. 2001-02-0106, Para 6 of the Concluding Part*).

13.1. Any restriction of fundamental rights should be based on conditions and argumentation about its necessity. Consequently, the restriction is set because of important interests – with a legitimate aim (*see: Judgment of 2 February 2010 in the case No. 2009-46-01, Para 11*).

Pursuant to Section 6 (1) of the Employees Protection Law, resources of the employee claims guarantee fund shall consist of: 1) a share of the State entrepreneurial risk fee; 2) gifts and donations; and 3) amounts recovered by administrators. In fact, the Guarantee Fund functions based on the self-funding principle. Resources of the fund are generally formed by State entrepreneurial risk fee that each employer pays for each employee on monthly basis. Consequently, claims against employers are satisfied from the resources of the Guarantee Fund that is constituted by the State entrepreneurial risk fee paid by the employers.

13.2. Section 7 (3) of the Employees Protection Law provides: "If the resources of the employee claims guarantee fund are not sufficient to satisfy employee claims in accordance with this Law, the employee claims shall be satisfied from the State budget in accordance with procedures prescribed by law." Although the Law envisages a possibility to use additional resources from the State budget to satisfy employees' claims, such mechanism shall be regarded as an exception from the general procedure and is admissible only in case of extreme necessity. Consequently, the task of the legislator is to ensure effective functioning of the Guarantee Fund, balancing of its income and expenses to assure satisfaction of all employees' claims in the long term in accordance with the Employees Protection Law.

Consequently, the necessity to balance income and expenses of the Guarantee Fund to ensure satisfaction of all employees' claims and avoid all expenses from the State Budget, namely, assuring protection of the rights of other persons and thus also welfare of the society, shall be regarded as a legitimate aim.

14. To evaluate whether the legal norm, adopted by the legislator, complies with the proportionality principle one has to ascertain: 1) first , whether such action is indispensable, namely, whether the legitimate aim can be reached by other means that would restrict rights and legal interests of a person at a lesser extent; 2) second, if such an activity is required, i.e., if it is not possible to attain the objective by other means, which would less limit the rights and legal interests of an individual; 3) third, if the activity of the legislator is proportionate or adequate, i.e., if the benefit, obtained by the society, is greater than the loss incurred to the rights and lawful interests of an individual. If, after evaluating the legal norm, it is acknowledged that it does not comply with even one of the above criteria, then it shall be considered as not being in conformity with the principle of proportionality and illegitimate.

14.1. The Saeima and the Cabinet of Ministers indicate that, during the economic recession in 2009, income from the State entrepreneurial risk fee reduced by 20 percent if compared to the planned one, whilst the number of claims to be satisfied was greater than the planned one. In 2009, it was planned to satisfy 1087 employees' claims, though in fact 2015 were satisfied, which is by 47 per cent more (*see: Case materials, Vol. 57, and 166*). In subsequent years, taking into account economic prognosis, no considerable increase of income from the State entrepreneurial risk fee was planned. Para 5 of Chapter III of the Annotation to the draft Amendments, one can find information on changes in income and expenses of the Guarantee Fund, which was considerably influenced by the economic situation in the State and rapid fall of employment rate. When establishing restrictions to employees' claims, social stability would be ensured in the long term in the

frameworks of resources available for satisfaction of employees' claims (*see: Case materials, Vol. 96 – 102*).

Taking into account the fact that resources of the Guarantee Fund are being used for satisfying employees' claims in case of insolvency of the employer, as well as the fact that the Guarantee Fund functions based on the self-financing principle, restriction of disbursements form the Fund shall be regarded as an appropriate solution, by means of which the legislator is able to assure reaching of the legitimate aim.

14.2. The Applicants indicate that the legislator has failed to property assess whether the legitimate aim could be reached by other means that would restrict the rights and interests of persons at a lesser extent, for instance, by increasing the State entrepreneurial risk fee or reducing expenses of the Insolvency Agency and remuneration of administrators.

When selecting any measure, the legislator is committed to consider whether legitimate aim may be reached in a more lenient way. The Constitutional Court emphasizes that a more lenient measure is not any other measure but the one that assures reaching of the legitimate aim at least at the same quality (*see: Judgment of 13 May 2005 by the Constitutional Court in the case No. 2004-18-0106, Para 19 of the Findings*).

The State has executed a range of measures to reduce expenses of insolvency proceedings. When the Cabinet of Ministers, on 21 April 2009, amended 11 December 2007 Cabinet Regulation No. 865 "Procedure, according to which costs and administrator's remuneration are covered in case of insolvency of a legal person from the resources of a State agency "Insolvency Administration" meant for this purpose", remuneration amount of the administrator was considerably reduced. Likewise, in 2009, the State executed large-scale reforms to reduce expenses from the State budget not only in respect to protection of employees in case of insolvency of the employer, but also in other fields.

In several judgments, the Constitutional Court has concluded that, during economic recession of Latvia in 2009, the State had to considerably reduce budget expenses (*see, e.g.:*

Judgment of 18 January 2010 by the Constitutional Court in the case No. 2009-11-01). Consequently, the legislator avoided increase of expenses from the State budget.

Selection of measures to reach the legitimate aim falls within the scope of competence of the legislator. If the legislator has considered what measure would ensure reaching of the legitimate aim and decided on restriction to be imposed on a certain group of persons, then such measure that imposes restriction on another group of persons cannot be regarded as a lenient one. Consequently, when assessing compliance of the Contested Norms with the fundamental rights established in the Satversme, the Constitutional Court can only verify whether the measure selected by the legislator restricts or not the fundamental rights of a person in a non-proportional manner.

The Constitutional Court also draws attention of the legislator to the fact that functioning of the Guarantee Fund is based on self-funding principle. State budget resources can be used only in case if the Guarantee Fund lacks resources. During the period from 2003 to 2009, the State entrepreneurial risk fee has been reduced threefold, namely, from nine lats to three lats per each employee on annual basis. It follows from the case materials that the State entrepreneurial risk fee has been reduced because the Free Trade Union Confederation of Latvia regularly (each year before the State entrepreneurial risk fee was confirmed by the Cabinet of Ministers) expressed objections against "groundlessly frozen financial means that have already been accrued at large amounts during the first three years when the State entrepreneurial risk fee was started to be collected" rather than the fee being to excessive and burdening for employees (*see: Case materials, pp. 125*). Consequently, the Guarantee Fund had necessary resources that were utilized after reducing incomes and increasing expenses. Consequently, when assessing the necessity of the contested restriction, the legislator has to consider the possibility to establish such State entrepreneurial risk fee that would assure functioning of the Guarantee Fund in the long term and without using State budget resources.

14.3. The Applicants indicate that the benefit gained by the society is not greater than the detriment caused to rights and interests of an individual, provided that the contested regulatory framework has considerably deteriorated their financial status.

However, in fact, the legislator has not refused satisfying employees' claims in case of insolvency of the employee; it has only restricted the amount of compensation during the transition process. This is permitted with Article 13 of the Convention No. 173 concerning the protection of workers' claims in the event of the insolvency of their employer and Article 4 of the Directive 2008/94/EC. The above mentioned legal acts emphasize that the guarantee sum cannot be less than the socially acceptable level. Pursuant to Recommendation No R180 of the International Labour Organization, where the amount of the claim protected by a privilege is limited by national laws or regulations, in order that this amount should not fall below a socially acceptable level it should take into account variables such as the minimum wage. Likewise, one should also take into account the fact that, in case of unemployment, these persons have the right to social unemployment benefit. Moreover, employees do not lose their right to claim against the employer in respect to outstanding sum, and pursuant to the Insolvency Law, such claims are regarded as prior ones if compared to claims of other creditors. Consequently, in case of insolvency of the employer, the right of the employees to receive these means are not denied.

The Contested Norms provide the possibility to satisfy, at a limited extent, claims of all persons who have the right to it pursuant to normative acts. Moreover, the restriction is terminated, namely, it last from 10 July 2009 to 31 December 2011. Consequently, benefit gained by the society is greater than the detriment caused to rights and legal interests of a person.

Consequently, the Contented Norms do not contradict the principle of equality included in the first sentence of Article 91 of the Satversme.

15. The Applicants hold that the Congested Norms do not comply with the principle of legitimate expectations that follows from Article 1 of the Satversme. Normative regulatory framework on protection of employees' claims in case of insolvency of the company has been amended after the company wherein the Applicants were employed was declared as insolvent.

The principle of legitimate expectations means that a person can trust into the fact that the rights and legal interests once granted would not be denied later. The basis of the principle is trust of a person into lawful and consequent actions of the State. The main duty of the principle of legitimate trust is to protect the rights of a person in cases, when – as the result of amendments to legal regulation – the legal status of an individual is or may be worsened (*see: Judgment of 8 November 2006 by the Constitutional Court in the case No. 2006-04-01, Para 21*). However, the principle of legitimate expectations does not exclude the right of the State to amend effective legal regulatory framework (*see: Judgment of 1 December 2010 by the Constitutional Court in the case No. 2010-21-01, Para 19*).

Consequently, in order to assess whether the new legal regulatory framework infringes or not the principle of legal security, the following should be investigated:

1) whether a person has been conferred legal security to safeguarding or implementation of any particular rights; and

2) whether a reasonable balance between protection of legal security of a person and ensuring of interests of the society has been observed (*see: Judgment of 26 November 2009 by the Constitutional Court in the case No. 2009-08-01, Para 23*).

16. In order to establish whether persons had the legitimate trust into preservation of exercise of certain legal norms, it is necessary to assess whether their trust into the Contested Norms is lawful, grounded and reasonable and whether the legal regulation in its essence is sufficiently well determined and unchangeable so that one may rely on it (*see: Judgment of 19 March 2002 by the Constitutional Court in the case*

No. 2001-12-01, Para 3.2 of the Findings, judgment of 25 October 2004 in the case No. 2004-03-01, Para 7 and Judgment of 8 November 2006 in the case No. 2006-04-01, Para 21).

The Employees Protection Law has come into effect on 1 January 2003. Up to 31 December 2004, the legislator had restricted the maximum amount of disbursement from the Guarantee Fund, whilst from 1 January 2005 claims have been satisfied at full extent. The right of employees to protection in case of insolvency of the employer, in fact, have not been amended since 1 January 2005. Consequently, persons did have legitimate, grounded and reasonable trust into exercise of the particular rights.

Consequently, the legal regulatory framework, in fact, was definite and unchanging enough.

17. When assessing the extent at which legal security of persons should be safeguarded, it should be taken into consideration whether the legal norm that has conferred the particular rights has already been applied to the persons. The extent of safeguarding of legal security differs depending on the fact whether a person has trusted into already conferred rights or those to be conferred (*see: Judgment of 26 November 2009 by the Constitutional Court in the case No. 2009-08-01, Para 25*).

When assessing whether the contested regulatory framework infringes or not legitimate trust of persons whose applications for satisfying their claims submitted to the Insolvency Administration before coming into force of the contested regulatory framework, namely, 10 July 2009, it is important to determine the date when persons were granted the right to satisfying their claims from resources of the Guarantee Fund.

Pursuant to the Insolvency Law, creditors' claims are submitted only after initiation of insolvency procedure. However, the administrator decides on recognition and inclusion of the above mentioned claims into the claim registry. After having performed respective actions, the administrator, based on Section 10 of the Employees Protection Law, submits

an application to the Insolvency Administration that adopts the final decision regarding satisfaction of the claims. Consequently, the right to disbursement of a certain sum from the Guarantee Funds is granted only after the Insolvency Administration has adopted a respective decision.

However, a legal norm that has not yet been applied may give grounds for a protected legal trust if it establishes prospective right, namely, the right have been already foreseen in a legal act, though not all prerequisites have set in for exercise thereof. Such legitimate trust occurs especially in case if a particular legal norm applies to already existing legal relations.

Consequently, the fact that, at the moment of adoption of the Contested Norms, the employees' claims have not yet been summarized in the administrator's application whilst insolvency of a particular company has already been declared, does influence the level of protection of legitimate expectations rather than determines whether legitimate expectation could have occurred.

Consequently, persons could trust into the fact that, after declaring the company insolvent, legal relations already existing would be dealt with pursuant to the legal regulatory framework that was effective on the date of declaring the company insolvent.

18. The Constitutional Court has already indicated that the principle of legitimate expectations shall be related with the necessity to create such circumstances that would permit a person to plan his or her future. Legal regulation shall be stable so that an individual, guided by legal norms, could adopt not only short-term decisions, but also make long-term plans for future (*see: Judgment of 25 October 2004 by the Constitutional Court in the case No. 2004-03-01, Para 9.2*). Establishment of a reasonable term or provision of compensation is generally applicable to cases when a person is deprived of or restricted rights already granted or anticipated. If exercise of the rights of a person

depends on a certain precondition that cannot be fulfilled in the nearest future or it is likely that it would never be fulfilled, no lenient transition is necessary and it can be substituted by other mechanisms (*see: Judgment of 30 March 2011 in the case No. 2010-60-01, Para 12.4*).

When introducing the Contested Norms, no transitional period was established. However, at the moment when they were adopted, as well as shortly before that, insolvency procedures were initiated in respect to many companies.

Insolvency procedure of a legal person is a body of legal measures, in the frameworks of which creditors' claims are covered by means of property of the debtor by thus facilitating execution of liabilities of the debtor. The procedure is launched on the date when the court has adopted a decision regarding initiation of an insolvency procedure, and it lasts up to the date when the court adopts a decision regarding termination of the insolvency procedure. Since insolvency procedure is a body of several measures and execution thereof requires certain time, the legislator, when establishing restrictions in respect to disbursements from the Guarantee Fund, had to assess the rights of all persons involved in the insolvency procedure disregarding the stage of a particular insolvency procedure.

It follows from the case materials that the Saeima Legal Office, when submitting an opinion on the draft Amendments to the Saeima Social and Labour Affairs committee on 15 May 2009, has drawn attention to non-compliance of suggested amendments with the principle of legitimate expectations: "The draft law envisages a norm on restriction of the amount of employees' claims, and it should be thoroughly assessed in relation to the principle of legitimate expectations existing in a democratic state. Also in laws determining social guarantees could be amended; however, the Constitutional Court has indicated in several judgments that the principle of legitimate expectations requires that the legislator, when introducing amendments into a law, would consider and establish a lenient transitional period to a new regulatory framework. In such cases, it is necessary to determine reasonable terms for meeting new requirements or to provide compensation of

losses incurred. The Legal Office has no information at its disposal regarding the status of all financial resources of the State; therefore it cannot made a conclusion that the option suggested in the draft law is the most lenient way for assuring social stability in the long term to satisfy employees' claims at the amount of available resources. [..] in fact it has a retroactive force" (*see: Case materials, pp. 103 – 104*). Consequently, the legislator's attention was drawn to infringement of the principle of legitimate expectations.

19. It also follows from the Directive 2008/94/EC that was transposed to the normative regulatory framework of Latvia that it applies to employees' claims against employers who have been declared as insolvent. However, it is emphasized in Article 2 of the Directive 2008/94/EC that an employer shall be deemed to be in a state of insolvency where a request has been made for the opening of collective proceedings based on insolvency of the employer, as provided for under the laws, regulations and administrative provisions of a Member State.

However, as the boundary for introduction of the new regulatory framework, the legislator has selected a certain activity in the frameworks of insolvency procedure rather than the date of initiating insolvency procedure, the first being submitting of an application of the administration that serves as the basis for the Insolvency Administration to adopt a decision.

The normative regulatory framework does not establish any particular term for submitting of such application. The administration can submit an application regarding satisfying of employees claims to the Insolvency Administration no earlier than after creditors' meeting of the insolvent employer where they adopt a decision regarding solution of insolvency, and no later than the date when the creditors' meeting of the insolvent employer adopts a decision regarding termination of insolvency procedure. Consequently, the right to disbursement from the Guarantee Fund are related with actions of the administrator. This means that it is probable that after initiation of insolvency procedure,

employees' claims in different companies are summarized in different terms based on workload of the administration. Consequently, no objective criterion exists determining the term for establishing restrictions in respect to disbursements from the Guarantee Fund.

When adopting the Contested Regulatory Framework, the legislator has protected the rights of only those persons who had already addressed the Insolvency Administration, and it has applied the previous normative regulatory framework to these persons. However, as to persons whose employees have been declared insolvent and whose claims have not yet been submitted to the Insolvency Administration before coming into force of the Contested Norms, the legislator has not established any transitional period and thus has infringed the principle of legitimate expectations.

Consequently, the Contested Norms, insofar as they apply to persons whose employer has been declared insolvent before the date of coming into force of the Contested Norms, fail to comply with Article 1 of the Satversme of the Republic of Latvia.

The Ruling

Based on Article 30 – 32 of the Constitutional Court Law, the Constitutional Court

h o l d s :

1) Para 6 and Para 7 of Transitional Provisions of the Law "On Protection of Employees in Case of Insolvency of Employer" insofar as they apply to persons whose employer has been recognized as insolvent before 9 July 2009 fail to comply with Article 1 of the Satversme and shall become null and void as from the date of adoption thereof;

2) Para 6 and Para 7 of Transitional Provisions of the Law "On Protection of Employees in Case of Insolvency of Employer" comply with Article 91 of the Satversme of the Republic of Latvia.

The Judgment is final and not subject to appeal.

The Judgment shall come into force on the date of publishing it.

Presiding Judge G. Kūtris

Translated by E. Labanovska, translator of the Constitutional Court