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The 'Trends & Developments' sections give an overview of current trends and developments in local legal markets. Leading lawyers analyse particular trends or provide a broader discussion of key developments in the jurisdiction.

Trends and Developments

Contributed by Brandl & Talos Rechtsanwälte GmbH

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Guilty Until Proven Innocent - Administrative Prosecutions in Austria

The Austrian administrative penal law is, in its current structure, a relic of the beginning of the 20th century which was designed to handle petty offences. The defendant only has very limited rights when engaging in his defence and – in essence – has to prove his innocence to an administrative authority that is judge, jury and executioner. Since the EU has relied on substantial administrative fines as one of its preferred method of harmonisation in recent years – particularly in the field of banking and capital markets law – managers in Austria are faced with an inconsistent and precarious situation. Threatened with administrative fines which can range into the millions of euros based on European regulations and directives, defendants subject to Austria's administrative penal law are forced into an unequal and weak position in the proceedings. This fact has been widely criticised for years. Now, the Austrian legislator has finally reacted, but only to a certain degree.

A Law for Petty Offences

The Austrian Administrative Penal Act (*Verwaltungsstrafgesetz*) was designed to handle petty offences such as parking fines and speeding tickets by relegating them to fast, simple and standardised proceedings. The limitation of the defendant's rights of defence was deemed necessary in order to reduce the duration of the proceedings and to guard against a possible collapse of the administrative system given the number of cases that the system would face. The legislator was fully aware that these restrictions would conflict with the principles behind a rule of law and fair trial. However, since administrative authorities only imposed relatively small

fines, the limitation on the defendant's rights in this context was deemed to be constitutional.

For decades it was well-established jurisprudence that the kind and severity of sanctions to be imposed was the distinguishing criterion between the jurisdiction of the (ordinary) criminal courts and the competence of administrative authorities. Based on Article 91 of the Constitution, the Austrian Constitutional Court (*Verfassungsgerichtshof*) decided that certain fines exceeding (undefined) thresholds would fall under the exclusive competence of the criminal courts. In a judgment from 1995, the Austrian Constitutional Court deemed it unconstitutional for an administrative authority to impose a fine of EUR145,000.

All that changed in December 2017 when the Constitutional Court discarded its former jurisprudence and ruled it to be constitutional for an administrative authority to impose fines of up to several million euros. This decision was somewhat surprising to the legal community and intensified the political discussions regarding the need to reform the Administrative Penal Act. The Austrian legislator has responded to the criticism and has mitigated some of the hardships a defendant faces in administrative prosecutions.

We will get back to the decision of the Constitutional Court and current legislative changes after we take a closer look at the relevant procedural provisions and the new standards stipulated by European law that lead to significant incongruencies in the administrative legal system.

The Peculiarities of Administrative Prosecutions in Austria

A very common misconception in the current public debate on administrative fines is that the fines are imposed on companies. Actually, the responsibility for compliance with the provisions of the administrative law rests collectively with the legal representatives of the company (eg, the managing directors or board members), unless special representatives are appointed for certain areas. Even though it is, at least in the majority of cases, the company and not the management that 'profits' from administrative offences, Austrian administrative penal law generally does not recognise the concept of corporate liability in this context.

It should also be noted that even slight negligence results in penal liability. This fact has considerable weight when considering that Austrian administrative penal law does not afford the presumption of innocence and in dubio pro reo. In reality, the approach is not 'innocent until proven guilty', but 'guilty until proven innocent'. Negligence is automatically presumed when the law is violated.

This leads to a fundamental difference in criminal law and creates a substantial disadvantage to any defendant that faces an administrative proceeding. Moreover, the administrative authorities and courts have set exceptionally high standards to prove that the defendant is not guilty of having violated the provision of the administrative law. The defendant needs to provide evidence that compliance with the relevant provision was impossible for reasons beyond his control and must further prove that he has taken all suitable and reasonable measures to prevent any violations. This requires an effective control system that ensures compliance at all times. According to the Austrian Administrative High Court (*Verwaltungsgerichtshof*), a control system is only to be deemed effective if the management has, inter alia, ensured that:

- all technical possibilities have been fully utilised;
- instructions are actually received and complied with down to the very lowest hierarchy level;
- any violations against instructions have been sanctioned internally; and
- there are regular controls regarding compliance at all levels.

In short, the standards for a sufficient control system are set unrealistically high so that they are not met in 99.9% of all cases.

Another factor that works to the disadvantage of any defendant is the so-called principle of inquisition (*Inquisitionsprinzip*). This means that violations of administrative law are not prosecuted by public prosecutors but by the same authorities that are responsible for enforcing the administrative law. A defendant is not in a position to plead his case to an independent judge but has to persuade the very authority that has initiated the proceedings against him of his innocence.

Another peculiarity of the Austrian administrative penal law is the principle of accumulation of fines (*Kumulationsprinzip*). If a person has committed several, separate administrative offences or if an offence is subject to more than one sanction, the offences are not considered as one offence, rather all fines are imposed cumulatively. This may sound logical at first, but the accumulation of fines can – in extreme cases – lead to excessive fines that are no longer proportionate to the gravity of the offences. This is best exemplified by the Andritz case.

The Andritz Case

Andritz AG is a Styrian mechanical engineering company. In 2015 Andritz AG ordered installation works from a Croatian company for the emergency repair of an industrial boiler that had exploded. The order volume was around EUR7 million. While Andritz AG considered this to be a simple service contract, the regional administrative authority (*Bezirkshauptmannschaft*) considered the contract to constitute personnel leasing and, therefore, to violate two provisions of Austrian Labour Law.

To provide an idea of the excess that such an accumulation of fines can amount to, in this case the regional administrative authority calculated the fine as follows: it considered two violations of Labour Law provisions, each valued at about

EUR12,000 for each of the four board members in over 200 cases (number of workers of the Croatian company). The regional authority imposed a total fine of EUR22 million on the members of the board of Andritz AG.

It is fairly obvious that fines of this magnitude threaten the livelihood of people and appear highly disproportionate to the gravity of the offence. This applies even more so when considering that the maximum corporate liability under Austrian criminal law based on the statute on responsibility of legal entities (*Verbandsverantwortlichkeitsgesetz*) amounts to merely EUR1.8 million.

Reimbursement of Fines

There is another common misconception about administrative fines. That is that fines imposed on management are always reimbursed by the company. While it may often be the case that companies do not leave their management out in the rain and are willing to reimburse their management for fines incurred, this is not always the case.

In particular, there is no legal obligation for companies to reimburse any fines to its management and any contractual clauses that stipulate such an obligation are deemed null and void (nevertheless, in practice such clauses can still be found regularly in employment contracts of managing directors and board members). Moreover, it is only admissible for a company – based on a decision by its supervisory board or shareholders – to pay fines of its management on a voluntary basis if the following requirements are met:

- The decision is made after the fine has been imposed;
- Before taking a decision, the case has to be assessed and discussed in detail, particularly if the actions and decisions of the management were based on a reasonable (legal) opinion. Moreover, the economic situation of the company and previous fines of the management need to be considered;
- The payment of the fine has to be in the best interest of the company.

If fines are reimbursed when these requirements are not met, the supervisory board or shareholders may expose themselves to liability towards the company. In addition, the tax implications of the reimbursement have to be considered. As there is no legal obligation for the company to reimburse its management for fines, any voluntary payments made are taxable income at the management level. Therefore, considering the maximum income tax rate of 55%, a company may have to pay more than twice the amount of the actual fine in order to fully indemnify its management. In the example of Andritz AG, this would amount to a payment of up to EUR49 million.

European Standards and National Gold-Plating

The European Union has relied on substantial administrative fines as a preferred method of harmonisation in recent years, particularly in the field of banking and capital markets law. EU regulations and directives such as, inter alia, the MAR (Market Abuse Regulation), CRD IV / CRR (Capital Requirements Directive IV / Capital Requirements Regulation) or the TD (Transparency Directive) stipulate maximum administrative fines of up to several million euros. The European legislator, with its intent on harmonising these areas of law, regards substantial fines as an effective way to ensure the proper enforcement of these rules in all member states.

In spite of this, the national procedural law of the member states has not been harmonised. In Austria this has led to the current situation, in which administrative fines of up to several million euro are enforced based on the Austrian Administrative Penal Act which is – as already shown above – clearly only suited for petty offences. Fines of this magnitude have been unheard of in Austria's administrative penal law and would certainly have been regarded as unconstitutional. However, since the European law generally has primacy of application and supersedes all forms of national law in conflict, national authorities must observe and implement all EU standards, including such fines, even if such application is deemed unconstitutional.

An additional problem results from the inaccurate and superficial manner in which European legal provisions and standards are transposed into Austrian law by the national legislator. In many cases this results in so-called 'gold-plating'. This results in an (often unintentional) excessive implementation of European law into national law by the legislator of the member state. A good example of gold-plating in Austria is the amendment of the penal provisions contained in the Austrian Banking Act (*Bankwesengesetz*) based on the requirements set out in the CRD IV (Capital Requirements Directive IV).

The CRD IV required the national legislator to implement maximum penalties of up to EUR5 million for natural persons in case of certain severe violations such as operating a bank without a banking licence, obtaining a banking licence based on false information or repeated offences in meeting capital requirements. The Austrian legislator transposed these requirements into the Austrian Banking Act in a way that subjected all violations against provisions of the Austrian Banking Act to the same maximum penalty of EUR5 million. This includes, for example, simple reporting duties regarding a change of the person responsible for the internal audit. It seems highly unreasonable that the law does not differentiate between major and minor violations.

The following case exemplifies what effect the combination of an inadequate administrative penal law and the flawed transposition of a European directive into national law can have for a defendant. In a case that was widely covered by the media, the Austrian Financial Market Authority (FMA) decided to dismiss two bank directors and claimed that they did not fulfil the personal requirements to qualify as 'fit and

proper' for the job. It is obvious that the ability to dismiss a bank director is one of the most intense interventions that the FMA as competent supervisory authority has at its disposal. The dismissal had a significant impact on the bank directors, who suffered financial and reputational damage affecting their future careers.

The European legislator was fully aware of these consequences and has therefore foreseen in the CRD IV that the bank director may personally appeal against his dismissal. In its transposition of the CRD IV into national law, the Austrian legislator did not, however, expressly mention this right of appeal in the Austrian Banking Act. As a consequence, the bank directors were denied standing in their own dismissal proceedings.

The currently prevailing case law of the Austrian Constitutional Court even confirms this interpretation, arguing that there are merely 'economic reflex effects' (as a result of the termination of an employment contract), but no conflicts with relevant constitutionally guaranteed rights such as the right to a fair trial. This does not take into account that during the recall process the personal reliability of the bank director is assessed. A negative decision has grave consequences for the bank director concerned, who – without being able to defend himself against the authority's claims – is hindered in his professional advancement and is threatened with existential consequences. In our opinion, the national legislator needs to address this issue in order to comply with the rule of law and fair trial requirements.

A Change of Mind

As already briefly mentioned above, the Austrian Constitutional Court discarded its former jurisprudence in this context with a decision from December 2017. For decades it was well-established jurisprudence that the kind and severity of sanctions to be imposed was the one distinguishing criterion between the jurisdiction of criminal courts and the competence of administrative authorities. Fines exceeding certain (undefined) thresholds were considered to fall into the exclusive competence of the criminal courts based on Article 91 of the Constitution. In a judgment from 1995, for example, the Austrian Constitutional Court deemed it unconstitutional for an administrative authority to impose a fine of EUR145,000.

In its decision from December 2017, the Constitutional Court (in essence) concluded that the delimitation of competences between the criminal courts and administrative authorities requires a broader approach than merely considering the magnitude of fines. Instead, the court argued that the additional following factors need to be considered:

- the general function and preventive effect of applicable fines (which may differ in criminal law and administrative penal law);
- the differences between legal and natural persons as addressees of laws;
- the fact that Austria has established independent administrative courts in 2012 to improve the legal protection in administrative proceedings.

Therefore, the Constitutional Court deemed it constitutional for the FMA as an administrative authority to impose fines up to millions of euros in the relevant case. This, however, does not change the fact that certain sanctions fall exclusively under the competence of the criminal courts based on Article 91 of the Constitution. It just changed and broadened the basis that the delimitation of competences between the criminal courts and administrative authorities is made on. At first, the decision of the Constitutional Court was perceived as a surprise in the legal community. Generally, the decision was received positively, as there are some comprehensive reasons to support the arguments of the Constitutional Court that the delimitation of competences needs to be assessed based on a broader approach. But as much as the decision of the Constitutional Court has been discussed in recent months, it has not changed two fundamental problems in this context:

- the delimitation of competences between the criminal courts and administrative authorities has, if anything, become more complex and unclear considering the broader approach set out by the Constitutional Court;
- the Austrian Administrative Penal Act still remains in force with all its deficiencies and limitations regarding the defendant's rights of defence, which conflicts inter alia with fair trial requirements and the rule of law.

Legislative Changes and Prospects

The wave of European regulations and directives stipulating administrative fines up to several millions of euros – particularly the General Data Protection Regulation (GDPR) that affects the majority of businesses in the EU – have intensified the public and political discussions regarding the need for a reform of the Administrative Penal Act even more.

The Austrian legislator has responded to the criticism and mitigated some of the hardships a defendant may face in administrative proceedings. Unfortunately, the legislator did not revise the Administrative Penal Act as a whole, but rather took a patchwork approach which led to a decision to discard the principle of accumulation of fines (*Kumulationsprinzip*) – which can lead to excessive fines in some cases – for individual administrative fines exceeding EUR50,000 and generally within the fields of competence of the Financial Market Authority. In addition, the FMA is now (expressly) entitled to refrain from imposing fines in certain minor cases. On the one hand, this is a significant improvement for banks, insurers, pension funds and security issuers. On the other hand, it clearly constitutes an unequal treatment of all other addressees of administrative penal laws.

The Austrian legislator is called upon finally to address these issues and to revise the Austrian Administrative Penal Act as a whole. Currently, managers are still faced with an inconsistent and precarious situation. While being threatened with administrative fines of up to millions of euros based on European regulations and directives, defendants are still left in an unequal and weakened position during the proceedings. It is about time to remedy these deficiencies in order for administrative proceedings to comply with the principles behind the rule of law and the right to a fair trial.

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