TWO PAGER

Key facts about a specific employment law topic

Pusch Wahlig Workplace Law

Pseudo self-employment

1. **What is pseudo self-employment?** Pseudo self-employment is the term used if, according to the underlying agreement, independent services or work for another company are to be provided by a contractor, but there is actually non-independent work in an employment relationship. Within the framework of the pseudo self-employment examination, a distinction must be made between the assessment under labour law and social law (and tax law):

- In employment law, employees must be distinguished from freelancers (sec 611a Civil Code)
- In social law, however, the question arises as to whether an activity constitutes work subject to social security contributions within the meaning of sec 7 para 1 Social Code IV

The concept of employee and worker is not identical. However, the labor law and social law's determination of an employee's status often leads to the same results.

2. **When does pseudo self-employment exist?** In both constellations, the decisive factor for differentiation is whether the employee is involved in a third-party work organization and is subject to the contractual partner's right to issue instructions. This may concern the content, implementation, time, duration and location of the activity. An overall weighing of each of the individual characteristics must be carried out. The decisive factor is the actual circumstances to the extent that they deviate from the "on paper" agreement.

The consideration of labour law is essentially the right of instruction. In short: the further the right of instruction extends, the more likely there is the existence of an employment relationship. In the social law assessment, on the other hand, all processes and facts that shape the contractual relationship between the client and the employee are comprehensively assessed. This makes the tests time-consuming. The most common features are:

- Specifications of the client with regard to location, time and duration of the activity
- Specifications of the client with regard to the type and manner of service provision (in addition to determine the contractual benefits) and/or close checks by the client
- Whether the individual has a manager at the client who has the authority to issue instructions
- No distinction of the services of the individual in cooperation with own employees of the client
- Employees of the client take over the same activities as the individual
- Prohibition of competition and secondary employment
- Participation of the individual in internal events of the client
- Integration into the client's infrastructure (Workplace/ desk, business cards, phone extension, e-mail address, access to the intranet, canteen use, etc.)
- Lack of authorization of the individual to use third parties to fulfill the tasks
- Provision of work equipment by the client (company car, laptop, mobile phone, office supplies etc.)
- Time-based remuneration (not performance-related)
- No own capital investment by the individual (e.g. no own work equipment; no self-financed insurance; no own permanent establishment; entitlement to remuneration for times of absence)
- Individual was formerly a worker of the client
- No possibility for the individual to work for differentclients.

In the overall assessment, it is not only important to determine whether there are more characteristics for or against the existence of employment within the meaning of sec 7 Paragraph 1 Social Code IV but the individual criteria are also to be weighted differently according to the circumtances of the individual case.

3. What are the consequences of incorrect assessment? The consequences of an incorrect assessment as to the existence of an employment relationship and the social status of an employee should not be underestimated. In the event of an employment relationship, a reason for termination of the contract is usually required under the Dismissal Protection Act. All other employee rights (paid leave, continued remuneration in the event of illness, working time law, minimum wage etc.) also apply.

In the event of an incorrect assessment of the status under social law, the subsequent payment of the social insurance amounts not paid (total social insurance contribution for pension, unemployment, health, nursing and accident insurance), regularly of both the employer and the employee contribution, are to be retrospectively repaid for 4 years. Furthermore, if there was intent to incorrectly determine the status of a worker the social insurance amounts may be required to be repaid for up to 30 years. In addition, there is a default surcharge of 1% of the amount in arrears for each commenced month of default. Paid amounts can only be recovered from the employee to an extremely restricted extent under statutory law (only the employee contribution for the last three months).

There are also risks under criminal and regulatory law. If an accident at work occurs, the Employer's Liability Insurance Association may demand full reimbursement of the expenses assumed (e.g. medical treatment and rehabilitation costs, injury allowance, injured person's pension, reintegration costs, widow's/widower's/widower's pension, etc., orphan's pension etc). The liability and criminal law risks affect the management personally. Therefore, any company, who works with freelancers must regularly check whether they are not only self-employed "on paper", but are actually self-employed.

4. What criteria apply to managing directors of limited liability companies? From a social law perspective, external managing directors (managing directors without capital shares) of a limited liability company are generally employed on a dependent basis. A managing partner of a limited liability company, on the other hand, is only in a dependent employment relationship if he (1.) takes part in the work process of the limited liability company in a functionally appropriate manner, (2.) receives remuneration for the activity and (3.) cannot exert any significant influence on the fate of the limited liability company by virtue of his share in the share capital. This shall only apply in the case of more than 50% of the share capital or by special agreement in the articles of association (blocking minority). The employee status of limited liability company managing directors, on the other hand, is judged differently. While the Federal Court of Justice assumes in its case law that a managing director is not an employee, according to the case law of the Federal Labour Court an employment relationship may exist in individual cases. The decisive factor is whether instructions are issued during the work and in a process-oriented manner (in the case of multi-person management). In these cases, a managing director may also be considered an employee under European law (inclusion of the scope of protection under the Maternity Protection Directive and of the Mass Dismissal Directive). If the managing director holds more than 50% of the capital shares or if he has a blocking minority, employee status will be generally excluded.