Contractor Compliance *Update* – BAG and BSG Rulings on Free Lancers as Regular Employees and on Illegal Employee Leasing

LATEST NEWS ON CONTRACTOR COMPLIANCE

The legally safe use of outside personnel continues to pose significant challenges for many businesses. In the context of **Contractor Compliance** concepts that are either already in place or are yet to be launched, there are a few detailed issues that have still not been settled, while others are constantly changing. Businesses thus cannot help but keep an eye on the current judicial rulings at all times to adjust their compliance concepts accordingly. This will particularly apply in cases where the highest courts address major detailed issues and thus provide practitioners with valuable information on what will work and what will not, which is what has happened in two more recent decisions of the Federal Social Court (*BSG*) and the Federal Labor Court (*BAG*) from January and March of 2017.

LEVEL OF COMPENSATION AS DIFFERENTIATING CRITERION (BSG JUDGMENT OF MARCH 31 2017 – B 12 R 7/15 R)

The first decision of the BSG concerns the ongoing **issue of how to distinguish** ostensible or de facto employment from self-employment. As we know, a number of individual criteria will determine this, particularly the duty to be bound by instructions and the integration of supposed freelancers into the principal's business organization.

In its decision, which has only been published so far in the form of a press release, the BSG adds the **level of the fee as a further indication**: *"For if the negotiated fee is significantly higher than the pay of an employee subject to the payment of social security contributions who has a comparable assignment (…) and this fee makes it possible to provide for personal coverage, this is a weighty indicator for an engagement as a freelancer."*

This statement is light on the horizon. The amount of a fee delivers, first of all, a relatively **unequivocal criterion** in the otherwise grey area of differentiating between employment and free lancing that is characterized by its evaluative aspects. One needs only to think in this context of the difference between (innocuous) activity-related instructions and (harmful) general employment-related instructions that can hardly be answered in a legally safe manner, at least not in borderline cases. Secondly, this decision provides hope, particularly for the wide area of so-called "knowledge workers" who often work in the **IT, consulting or other comparable industries** on the basis of freelance contracts for work and services or for services. In the case at hand, the BSG had deemed earnings of EUR 40.00 to EUR 41.50 per consulting hour to be sufficient, as this was significantly higher than the fees for comparable remedial teachers subject to social security contributions. As a rule of thumb, it is very likely that this requirement will be met in the case of so-called "knowledge work".

„ONE-MAN GMBH" AS A SUITABLE PROTECTIVE UMBRELLA? (BAG JUDGMENT OF JANUARY 17, 2017 – 9 AZR 76/16)

Another plus point in legal security - albeit in the other direction – is supplied by the decision of the BAG that is concerned with involvement of legal entities as middlemen. The appointment of a "**one-man GmbH"** or comparable instruments are often chosen by practitioners to protect against the risk of de facto employment or illegal employee leasing.

The BAG is now of the opinion that this kind of involvement can actually help. This was at least the case in the dispute at hand in which the self-leasing of the sole shareholder and sole managing director of a GmbH **is not supposed to fall under the Temporary Employment Act** (**AÜG**), at least not if the company has a license under the Act and also leases other employees to third parties as the lessor (and not as the managing director) under the scope of its business activity.

So far so good. However, if the first commentators infer from this that the idea of the "one-man GmbH" as a whole has been saved, they are going too far. This has already been indicated by the BAG when it states at great length at the end of the decision under the key word "**institutional legal abuse**" in its discussion of the "one-man GmbH" and makes clear that, in any event, a concept "*whose sole or primary purpose is to be able to employ the managing director in a position in which he must comply with the instructions of the principal while avoiding the creation of an employment relationship"* is an abuse of law.

HOLISTIC APPROACH NECESSARY

With respect to **Contractor Compliance** concepts that are already in place or are to be introduced, this means that a holistic strategy will remain the sole key to success. The increase of compensation levels or the interposition of legal entities does **not constitute a stand-alone cure-all** but may supply effective building blocks in an overall concept whose implementation in actual practice will continue to involve both agreements and individual measures.

In addition, caution should still be observed in the individual case. The (legally abusive) interposition of legal entities may entail **direct disadvantages** in addition to

administrative costs, particularly if this is overused. It can be assumed, at any rate, that the permanent assignment of numerous "One-man GmbHs" and "You, Inc.s" at a principal's location will give rise to a not quite unfounded skepticism on the part of administrative tax and social security auditors which can have a major impact on the findings of the audit.

On the other hand, the decision of the BSG is a ground for hope, particularly in the field of so-called "**knowledge work**". One must bear in mind in this context that more than 70 per cent of the approximately 2.5 million solo freelancers in Germany are engaged in research, technical work or comparable work. It was particularly in these areas that the reform act of the AÜG that came into effect in April gave rise to an uncertainty to which the German lawmaker have inadequately responded. The current decision of the BSG moves in the right direction. In light of the general concept of protection in social security law (protection of the economically and socially less privileged populations, cf. § 1 Social Code I) it is only right that **economic parameters** are included in the question of how to make a differentiation between freelancers and regular employees. Off the record, some social courts have already handled the issue in this way. Using the cut-off for the duty to pay social contributions as orientation could supply useful assistance to practitioners in the future.

But even in the area of well paid "knowledge work" the rule applies that the level of compensation can only supply one building block under the holistic approach. Still, the ruling should provide a little security and encourage those who have been doubting the **future feasibility of their work contract models** following recent political developments. Work and service contracts will remain major components of specialized market economies and, as far as the law is concerned, can be shaped individually, provided an adequate compliance concept is in place!

FURTHER INFORMATION

You can find further information on the topics of employee leasing and work contracts on our homepage under the heading **Contractor Compliance**.

We would be very happy to include you on the list of subscribers to our free newsletter.

Just send us a brief **Mail** with your request.

CONTACT

Dr. Thilo Mahnhold
t.mahnhold@justem.de

Dr. Daniel Klösel
d.kloesel@justem.de

www.justem.de