The engagement of external personnel and its risks

New case law from the Federal Court of Justice on the question of intent in cases of pseudo self-employment

By Henning Reitz and Dr. Daniel Klösel

Individuals involved in decisions regarding the engagement of external personnel should certainly be aware of this decision.

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The engagement of external personnel continues to be of enormous importance in operational practice. Although companies can hardly do without the engagement of external personnel — whether in the form of individual self-employed persons or in cooperation with independent service companies — the use of external personnel under German law is still associated with numerous legal risks. These risks mainly stem from the still imprecise demarcation between dependent employees and external personnel — a line that is difficult to draw, even for experienced lawyers. The core problem lies in the fact that employees who are not self-employed must be registered for social insurance by their employer and the employer shares responsibility for the payment of wage tax. At the company, if the decision-makers responsible for classifying employees wrongly classify individuals as self-employed, this introduces the problem of pseudo self-employment *(Scheinselbstständigkeit)*, leading to numerous legal risks. In these cases, in addition to the possibility of the company facing a potentially existence-threatening obligation to pay social security contributions in arrears, it may also be that the individuals at the company who are responsible for the misclassification (for example, managing directors or board members) can be prosecuted individually under criminal law and can be held liable under civil law for nonpayment of social security contributions.

Concerning this question of the personal liability of decision-makers responsible for misclassifications, the German Federal Court of Justice recently made a decision of high practical relevance in a criminal case. The decision opens the door for new defense strategies in event of a personal claim or criminal investigation. The specific question at hand addressed which requirements must be met in order for decision-makers at a company who are responsible for personnel misclassification to be accusable of "intentional" behavior.

Decision of the Federal Court of Justice on January 24, 2018, file No. 1 StR 331/17

The decision in this case was founded on accusations of withholding and embezzlement of wages (section 266a of the German Criminal Code), as well as tax evasion. The defendant had not registered the Polish craftsmen employed by his company who, under social law, should have been classified as employees and registered with the relevant social security collection agency. Conse-

quently, the defendant had not paid any social security contributions on behalf of these workers for a period of about two and a half years.

The District Court, which initially had jurisdiction for this case, acquitted the accused on the grounds he lacked intent in terms of his position as the employer. The revision of the public prosecutor's office against this decision was successful, and the case was referred back to the District Court by the Federal Court of Justice for a new trial and decision. In practice, however, this course of procedure was less important than the references made to the legal requirements of intent, and thus also of criminal liability, which the Federal Court of Justice expressly addressed to the lower District Court. The Federal Court of Justice essentially stated:

"In the absence of an objective reason for differentiation in the legal prerequisites of intent in a case of tax evasion (section 370, paragraph. 1, No. 2 of the Fiscal Code; section 41a of the Income Tax Act) on the one hand and the withholding and/or embezzlement of wages pursuant to section 266a of the German Criminal Code on the other, the Senate — contrary to the previous rulings of the Federal Court of Justice — is considering (also) treating the misconception about employer status in section 266a of the German Criminal Code and the resulting obligation to pay social security contributions as an error of fact in future."

Therefore, punishability no longer merely requires that the person responsible has a deliberate intention relating to the actual conditions that lead to pseudo self-employment; the intention must also relate to the legal classification of pseudo self-employment as such and to the resulting obligation to pay contributions!

Practical implications of the decision

The decision is a novelty in the case law of the Federal Court of Justice and of utmost practical relevance, especially for decision-makers within companies that employ freelancers. Although the question of demarcation — especially in borderline cases — could hardly be answered reliably by experienced lawyers (due to the large number of vague criteria, as well as the fact that the case law was not able to provide a reliable answer to the question of demarcation), previously the case law of the criminal courts put substantial pressure on company executives responsible for misclassification, even though these executives often were not legal experts regarding pseudo self-employment issues. According to the long-standing case law of the First Criminal Senate, "intent" with regard to the actual circumstances was sufficient (concerning the use of the contractor per se or the underlying modalities), while an incorrect legal assessment as a self-employed person was merely intended to justify an "error of prohibition," which was, however, regularly avoidable and thus irrelevant due to the possibility of conducting status proceedings pursuant to section 7a, paragraph 1, sentence 1 of the Social Code IV (cf. Federal Court of Justice from June 5, 2013 — file No. 1 StR 626/12).

However, the latest progress in case law does more than simply lead to a considerable expansion of the requirements for criminal liability and thus also to an expansion of the possible defense strategies associated with them. It also has two other significant consequences: First, criminal liability according to section 266a of the German Criminal Code had been a vehicle for the German Pension Insurance *(Deutsche Rentenversicherung)* to take action not only against a company, but also against the responsible executives themselves in connection with outstanding social security contributions (often in not inconsiderable six- or even seven-digit amounts). Second, the adoption of willful intent offered a further vehicle for the German Pension Insurance to increase the period of subsequent payment of social security contributions from four to 30 years, as well as to proceed with the calculation of the total amount from net wage agreements and add significant late payment fines.

Conclusion

This new case law at least lowers the risk associated with classification of personnel and provides a starting point for expanded defense strategies, not only with a view to possible criminal proceedings, but also in connection with civil liability issues, as well as in the context of the usual procedure against additional claims of the German Pension Insurance. It is already foreseeable that, by means of these new defense strategies, it may be possible to considerably reduce the liability costs in question. On the other hand, however, the case law also gives a direction for other legal changes in connection with alleged pseudo self-employment, because (long neglected) attribution questions are now being asked more and more frequently and can, in numerous cases, help to avoid the liability of companies and persons responsible.

Individuals at companies who are involved in decisions regarding the engagement of external personnel should certainly be aware of this decision. Further developments in this jurisdiction are eagerly anticipated. It remains to be seen whether further jurisprudence will continue along this path, finally eliminating the unreasonable risks faced by decision-makers in association with (mis-)classification of personnel. <-

Dr. Daniel Klösel,
Attorney-at-Law (Germany), Associated Partner,
JUSTEM Rechtsanwälte, Frankfurt am Main

d.kloesel@justem.de

Dr. Henning Reitz,
Attorney-at-Law (Germany), Partner,
JUSTEM Rechtsanwälte,
Frankfurt am Main

h.reitz@justem.de

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Dr. Guido Zeppenfeld, LLM
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Friedrich-Ebert-Anlage 35-37, 60327 Frankfurt am Main
T +49 69 7941 2241

Königsallee 61, 40215 Düsseldorf
T +49 211 86224 0

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