Tiefenbacher
ATTORNEYS | TAX ADVISERS

DOING BUSINESS IN GERMANY

July 2014

Tiefenbacher
ATTORNEYS | TAX ADVISERS

Table of Contents

Table of Contents **2**

A. Introduction **4**

B. General Information **4**

1. Area 4
2. Population 5
3. Politics 5
4. Work and Residence Permits 6
   - 4.1. EU Citizens (including Iceland, Liechtenstein, Norway and Switzerland) 6
   - 4.2 Non-EU Citizens 7

C. German Economy **9**

D. German Business Practices **9**

E. Business Infrastructure **10**

F. Establishing a new Business in Germany **11**

1. Limited Liabiltiy Corporation Company (GmbH) 11
2. Mini-Limited Liabiltiy Corporation Company (Unternehmergesellschaft haftungsbeschränkt, UG) 16
3. Stock Company (Aktiengesellschaft, AG) 17
4. Partnership limited by shares (Kommanditgesellschaft auf Aktien, KGaA) 20
5. European Public Limited Company (Societas Europaea, SE) 20
6. Partnerships 21
7. The Advantages of a Partnership compared to a corporate structure 23
8. Other 23

G. Taxation **24**

1. General information 24
2. Corporate Income Tax 24
3. Personal Income Tax 24
4. Trade Tax 25

H. German Labour Law **25**

1. Collective agreements 26
2. Workers council 26

3. Principle of Equal Treatment 26
4. Employment Contract 26
4.1 Interview 27
5.2 Employment Contract Contents 27
5.2.1 General Business Terms 27
5.2.2 Working Hours 27
5.2.3 Probationary Time 28
5.2.4 Limited-Term 28
5.2.5 Part.Time 28
5.2.6 Salary 28
5.2.7 Paid Leave 29
5.2.8 Sick Leave 29
5.2.9 Industrial Accident 29
5.2.10 Maternity Leave 30
5.2.11 Parental Leave 30
5.3 Termination of Employment 30
5.3.1 Limited-Term Employment Contract 30
5.3.2 Dismissal with the Option of Altered Conditions of Employment (Änderungskündigung) 30
5.3.3 Cancellation Agreement (Aufhebungsvertrag) 30
5.3.4 Termination of the Employment Contract by giving Notice 31
5.3.5 General dismissal protection 32
5.3.6 Particular Dismissal Protection 32
5.3.7 Employment Reference Letter 32
5. Labour Law Suits 33
6. Taxes and Social Insurance Contributions 33
7. Ostensible Self-Employment (Scheinselbständigkeit) 33

A. Introduction

The Federal Republic of Germany is not only the largest European economy and the fourth-largest economy in the world but also ranks amongst the world's top exporters. It therefore represents an attractive place with great prospects for foreign businesses. However, if you are considering doing business in another country it is essential to fully know and understand the local business environment, which might differ from the one you are used to. Against this background, this brochure aims to provide an explanatory guideline for foreigners on how to do business in Germany as well as to point out relevant German legislations. Nevertheless, due to the diversity of options and complexity of European and German legislations this can only be a general overview. On that score, Tiefenbacher specialises in business law across the broad range of areas essential to companies and investors doing business in Germany. With more than 40 professional staff, including certified public accountants and tax consultants in several locations in Germany, we have the capacity to deliver promptly efficient and targeted advice where it is required. Hence, if you have any further questions after reading this brochure, please do not hesitate to contact us. It will be our pleasure to assist you.

B. General Information

1. Area

The Federal Republic of Germany consists of sixteen different states and is located in Western and Central Europe. It covers an area of 357, 021 km2, which is dominated by a temperate seasonal climate. The bordering nations are Denmark, Poland, the Czech Republic, Austria, Switzerland, France, Luxembourg, Belgium and the Netherlands. The capital of Germany is Berlin.

2. Population

With approximately 80.8 million inhabitants, Germany is the most populous member state of the European Union. Moreover, its population is characterised by a certain cultural diversity due to the fact that almost 20 % of the inhabitants are people with an immigration background. The largest of these foreign nation groups are the Turkish followed by the Polish and the Russians.

However, Christianity represents the most prevailing religion in Germany with 62.8 million adherents. The second largest religion after that is Islam with an estimated 4.3 millions adherents, followed by Buddhism (300.000 adherents) and Judaism (100.000 adherents).

Although German is the official language in Germany, English is spoken by a wide range of people.

3. Politics

Germany is a federal, parliamentary, representative democratic republic. The current Federal Chancellor is Angela Merkel. She therefore heads the executive branch of government. Joachim Gauck whose responsibilities are mainly of a more representative matter is currently the President of Germany.

The German legislative power is divided between the Bundestag and Bundesrat. While the Bundestag is directly elected by the German citizens the Bundesrat represents the 16 different federal states of Germany. The Bundestag, that is more powerful in practice, is elected for a four year term and consists of 631 members. 299 of those members are elected in single-seat constituencies according to first-past-the-post. The other members

are allocated from statewide party lists put up by the parties themselves in order to achieve a proportional distribution.

In this context Germany's party system is dominated by the Christian Democratic Union (CDU/CSU), the Social Democratic Party (SPD), the Left (Die Linken) and Alliance 90 / the greens (Bündnis 90/ die Grünen). At present, the governing Parties are CDU/ CSU and SPD (Grand Coalition)

Germany has a civil law system. A so-called ordinary judicial branch, consisting of four levels up to the Bundesgerichtshof, focuses on civil and criminal cases. However, there are separate judicial branches for administrative, labour, finance and social security issues each with their own hierarchies. In addition to that, Germany has a powerful Federal Constitutional Court (Bundesverfassungsgericht) responsible for constitutional matters, with power of judicial review.

4. Work and Residence Permits

4.1. EU Citizens (including Iceland, Liechtenstein, Norway and Switzerland)

Due to the EU rules on the free movement of workers, citizens of EU Member States as well as those of the EEA and Switzerland have the right to live and work in Germany for three months as long as they hold a valid passport or a photo identity card. Therefore, no visa or work permit is required. Nevertheless, every new citizen must register with the police (polizeiliche Anmeldung) and the local residency office (Einwohnermeldeamt) of the local town hall if he or she is staying longer than two months. This registration has to be completed within two weeks moving in into a permanent accommodation. The following documents are required for the registration in question: A valid passport or a national identity card, a copy of lease or rental agreement and a completed registration form. After having made this registration a registration card will be issued. EU citizens are able to reside in a Member State for more than three months if they are entitled to freedom of movement. In principle, EU citizens are entitled to freedom of movement, especially for EU citizens who want to reside as workers in Germany seeking employment.

4.2 Non-EU Citizens

Non-EU citizens who intend to stay in Germany for less than 90 days must apply for a visa. But some citizens of certain states don´t need to have a visa. You can check the list of the countries whose citizens require a visa for entry into Germany at

http://www.auswaertiges-amt.de/DE/EinreiseUndAufenthalt/StaatenlisteVisumpflicht_node.html.

However, if they plan to stay for more than 90 days they must obtain a German residence permit. This can be made in conjunction with the above-mentioned visa application. Although, citizens of the United States, Australia, Canada, Israel, Japan, New Zealand and South Korea may apply for the needed residence permit after their arrival in Germany. Pursuant to the new German Immigration Act from 1 January 2005 this residence permit also gives foreigners the right to work in Germany (instead of separate residence and work permits). Nevertheless, after their arrival in Germany, non- EU citizens have to go through the same police registration procedure as described above.

Overall, it is to say that immigration to Germany for non-EU citizens is still limited to skilled workers (individuals with either a polytechnic or university degree or at least three years of training together with job experience) and students and their near relations.

However, there are four different types of residency permit: the limited resident permit (Aufenthaltsgenehmigung), the unlimited settlement permits (Niederlassungserlaubnis), the permission for permanent EU-residence (Erlaubnis zum Daueraufenthalt EU) and the Blue Card EU (Blaue Karte EU).

Limited resident permit: Once the registration process is completed a limited residence permit must be applied for within 90 days after the arrival in Germany. The local authority for foreigners (Ausländerbehörde) is the appropriate authority in this matter. The following documents are required for the application: Passport, two recent passport photographs, employment contract or student enrolment, evidence of financial support (student grant, bank statement etc.), proof of health insurance and a police registration form. Depending on individual circumstances (for example nationality, duration of employment contract or period of study) the validity of the limited resident permit can vary. Non EU citizens are only allowed to work if this is expressly noted on the limited resident permit.

Unlimited settlement permit: The unlimited settlement permit is an unrestricted permit for permanent residency. It is usually granted once a person has spent a certain period of time in Germany. However, occasionally it is granted immediately on arrival. This can be the case because of political reasons or because of the specific high qualifications of the citizen who contributes to the German labour market. An unlimited settlement permit usually requires the following criteria:

- having held a five year's residence permit
- Proof of being employed for at least five years and having paid the relevant social contributions
- Proof of ongoing financial support
- Proof of appropriate accommodation for the applicant and his family
- Adequate knowledge of the German language
- Basic knowledge of the German legal and social systems

Spouses are normally granted unlimited settlement permit on the basis of their partner living in Germany already (family reunification visa).Whereas children are usually granted the permit after they have been residents for at least five years.

Permission for permanent EU-residence: This is also a permanent residence permit. This permit entitles the non EU citizens to work. The conditions are similar to that for the unlimited settlement permit. Furthermore the permission for permanent EU-residence allows mobility within the EU. But not both – unlimited settlement permit and permission for permanent EU-residence - can be obtained for one person. Also foreigners with "refugee-status" are not able to get this permission.

Blue Card EU: The Blue Card EU is a temporary residence (four years) but only for non EU citizens with university degree or a comparable degree to find a job in keeping with their qualifications. An additional condition is the poof of an employment with a minimum annual salary of at least 47.600 Euro. EU Blue Card Holders who are working more than 33 months and who are paying premiums for pension get a permanent permit.

C. German Economy

The Euro, which is divided into 100 Cent, has been the official currency in Germany since 2002. The foreign exchange reference rates are published by the European Central Bank (ECB).

Manufacturing is the backbone of Germany's economy. The country is a member of the G-8 Group and therefore belongs to the richest nations in the world. One of Germany's most important industrial regions is the Ruhr which is an area of coal mines and steel mills along the Ruhr River. Other important industrial areas are located in Bavaria, Dresden and Hamburg.

Machine and vehicle construction as well as the chemical industry belong to Germany's most important industries. In this context, Germany's industries not only include the most famous cars, namely BMW, Volkswagen, and Mercedes-Benz but also worldwide exporting companies like Bayer, BASF and Hoechst. In addition to that, electrical engineering, electronics, and office equipment are growing industries in Germany.

Germany's economic success is mainly due to foreign trade. It exports a large amount of motor vehicles, chemical products, engineering articles as well as electrical engineering products. Nevertheless, most of the energy resources and raw materials for the German industries are imported, based on the fact that the country has only small amounts of natural resources. Other main imports are food, drinks, tobacco, and petroleum products.

In 2013 Germany's GDP was approximately 2.735,80 billion Euro (equals 3,593 billion US-Dollar).

D. German Business Practices

The normal working hours are from 9am to 5pm. However, the retail opening hours depend on the respective state and might vary. Nevertheless, 24h shopping on Sundays is only available on certain gas stations and at other sites relevant to travel.

In Germany the standard added tax rate is 19 %. However, there is a reduced tax rate of only 7 % that mainly relates to food and agricultural products. VAT is imposed on assets

and services in Germany and on imports into Germany. Overseas exports are except from VAT.

In comparison with other countries wages in Germany rank not only amongst the highest in Europe but also worldwide. In 2005 the average industry wages were 27,90 Euro in the western part of Germany and 17,40 Euro in the eastern part. Though, the quality of German labour and its efficiency is well-known throughout the world. Furthermore, in 2015 statutory minimum wages of 8,50 Euro will be introduced.

Average working hours are 37,5 hours per week and the annual leave varies between 20 and 30 working days. It has to be noted, that workers in Germany are protected by strong labour laws which entitle them to many different rights. For example the ordinary dismissal of workers must be proceeded by notice, which depends on the duration of the time the employee stayed with the company (it varies between 1-7 months.) In addition to that, unions are powerful and large in Germany. Social Security and Health Care costs are equally split up between the employee and the employer. (Please refer to the respective chapter “German Labour Law”)

E. Business Infrastructure

Germany’s infrastructure belongs to the most developed ones in the world. Especially with regard to EU requirements the German transport and communication utilities have been liberalized. The result is an efficient network of motorways, railways and waterways connecting Germany with major hubs in the world.

Germany has not only the third largest motorway network worldwide in length but also a well established network of high-speed trains. The InterCityExpress of the Deutsche Bahn AG (the national railroad carrier) serves major German cities and destinations in bordering countries

All together there are 40 airports in Germany. The biggest and busiest of them is the Rhein-Main airport near Frankfurt am Main (FraPort). However, other major airports with frequent air traffic are in Munich, Cologne-Bonn, Berlin-Tegel, Düsseldorf and Hamburg.

Germany also has a very well developed marine transport with major sea- and inland ports. In this context, the main sea ports include Kiel, Rostock and Lübeck on the Baltic

Sea and Emden, Bremen, Bermerhaven and Hamburg (the biggest of all ports in Germany) on the North Sea. Relevant river ports on the other hand are in Duisburg Cologne, Bonn, Mannheim and Karlsruhe on the river Rhine, in Magdeburg and Dresden on the river Elbe and in Kiel on the Kiel Canal which provides an important connection between the Baltic and the North Sea.

F. Establishing a new Business in Germany

Germany offers a broad variety of different legal forms for running a business. However, which of these legal forms a foreign investors should choose will depend on mainly individual factors such as functioning, capitalization, liability, accounting issues, and tax considerations.

There are three major forms of corporations under the German law:

- the Limited Liability Corportaion Company (Gesellschaft mit beschränkter Haftung-GmbH),
- the AG (Aktiengesellschaft) and
- the KGaA (Kommanditgesellschaft auf Aktien).

1. Limited Liabiltiy Corporation Company (GmbH)

The GmbH is the German business entity most commonly used by foreign investors. One reason for this is the fact that German law provides great potential, flexibility and freedom for adapting a GmbH to the individual needs of its shareholders. Therefore, the GmbH is especially suitable for small- and medium-sized businesses.

- **General Information**

A GmbH is a company with legal personality. It therefore can sue and be sued as well as hold and dispose of rights. Its legislation is the Limited Liability Companies Act. When it comes to naming a GmbH there are no restrictions apart from the fact that confusions with existing companies have to be avoided and the name must contain a reference to its limited liability by use of the abbreviation “GmbH” at the end of the name.

A GmbH can be formed for any rightful purpose. From a legal point of view it makes no difference if a GmbH is registered in a specific German state due to the fact that the German corporation law is federal law. However, tax rates may vary from location to location. (Please refer to the respective chapter “Taxation”).

- **Formation**

The first step on the road to form a GmbH is the notarization of a Deed of Formation and Articles of Association. This is usually be done by the founding shareholders. However, a representative of the founding shareholder(s) acting under power of attorney may conclude the notarized agreements.

Immediately after the above-mentioned notarization a bank account has to be opened by the company and cash contributions to the share capital must be deposited. Only after this has been done the company can be registered with the Commercial Register (Handelsregister). By doing so the Managing Directors must certify to the Commercial Register that the cash contribution is still at the company’s account and at their disposal at the time of filling in the applications. This registration for application has to be signed by all managing directors in person before a notary who not only certifies their signature but also instructs them about their duties as Managing Directors. This formation process usually takes between 3 - 12 weeks.

- **Company in Formation (Vor- GmbH)**

After having completed the first step of formation (notarization of the deed of formation and articles of association) the company already exists as a company in formation (Vor-GmbH). Although the company only becomes a separate legal entity after the registration with the Commercial Register it may start its business operations even at this stage. Rights or liabilities which arise from those activities done prior to registration are legally the rights and liabilities of the company in formation. However, upon registration the mentioned rights and liabilities acquired before the registration are assigned by law to the GmbH. It is important to note that the company’s net asset prior to registration must not be less than the amount of the registered share capital. If this is the case, the shareholders will be liable for the difference between the amount of the registered share capital and the net asset.

- **The Articles of Association**

The Articles of Association can be phrased in different ways depending on the degree of flexibility desired by the shareholders. Therefore, the Articles of Association may be formulated rather short only setting out mandatory provisions such as name, registered office, duration, registered share capital, purpose, initial contributions of the shareholders, representation and management of the corporation. Nevertheless, the Articles of Association can as well be a detailed description of the shareholder's rights and obligations, classes of shares and restriction on the transfer of shares

- **Registered Share Capital**

The minimum share capital for a GmbH is 25.000 Euro.

A GmbH is not obliged to issue share certificates or to keep formal records of share ownership. Instead of that, the ownership of each share is recorded only in the corporation deed. However, later transfers of share will be documented in transfer deeds attested by a notary. After each of those transfers of shares an up-dated shareholders' list must be submitted to the Commercial Register by the Managing Directors. Nevertheless those lists have mainly an informational function and do not provide evidence of the ownership of shares.

(1) How to transfer shares

The transfer of shares requires a notarized transfer deed. In addition to that, prior consent of the company is needed if only a part of a share shall be transferred. However, the Articles of Association may provide additional requirements which also have to be met by the transfer action (such as the consent of other shareholders).

(2) Contribution

The contribution to the share can be in cash as well as in kind.

In the event of the contribution being in kind, the Articles of Association must provide a specific form of the contribution and the exact amount of the corresponding share capital. The contribution must be worth at least as much as the above-mentioned corresponding share capital. Otherwise the shareholder is obliged to pay the respective difference in cash. Furthermore, the shareholders must hand in a report on the valuation of the contribution in kind. If the contribution in kind is another business, the financial results of the last two years have to be submitted too.

A cash contribution on the contrary requires that 50 % or 12.500 Euro (depending on which of these are greater) are paid up at the time of submitting the application for the company's registration. In the case of the company only having one shareholder additional security must be provided for any unpaid amount of the capital. If the contribution is in kind, this contribution must be submitted in full.

Furthermore, it is important to note that a GmbH is not allowed to make payments to the shareholder which might reduce the net asset below the amount of its registered share capital.

- **Managing Director(s)**

Any person with a full legal capacity can be appointed a Managing Director. The Managing Director belongs to the mandatory bodies of a GmbH. Nevertheless, a Managing Director neither needs to be a shareholder of the company nor a German resident. In the case of only one Managing Director being appointed she or he is the sole representative of the GmbH. Nevertheless, if more than one Managing Director is appointed they usually represent the company jointly (Furthermore, the shareholders may grant one or several Managing Directors to represent the company individually or represent the GmbH jointly with one or more other Managing Directors or with an authorized officer).It should be noted that the German law distinguishes between the appointment and removal of the Managing Director(s) on the one hand and his Service Contract (Dienstvertrag) on the other hand. These two issues are dealt with separately by the law.

The company's business is managed by the Managing Director(s) who apply the standards of a prudent business person to their dealings. However, additional obligations and duties of the Managing Director(s) may be constituted by the Articles of Association or the service contract. If the Managing Director(s) do not comply with their duties they are jointly and severally liable to the company. In detail this means Managing Directors must not disclose trade secrets of the company, they must ensure that the company keeps proper records, they must declare bankruptcy in the event of the company being overdept and if half of the share capital is lost, he must call a Shareholder's Meeting.

- **Shareholder's Meeting**

The Sharholder's Meeting which also belongs to the mandatory bodies of a GmbH is not only entitled to approve Managing Directors but also to remove them. It therefore has control over the management. In addition to that, the Shareholder's Meeting adopts annual financial statements as well as appropriates and distributes profits.

- **Supervisory Board**

In principle, a Supervisory Board is not necessary (unless otherwise agreed in the Articles of Association). However, if the company has more than 500 employees, a Supervisory Board becomes compulsory. In this case, a third of its members have to be employee's representatives. Only if the company counts more than 2000 employees half of the members of the supervisory board have to be employee's representatives.

The main function of a Supervisory Board is the supervision of the company's management. Other possible tasks are the appointment or removal of the Managing Directors and the adoption of the annual financial statement meetings.

- **Shareholders**

Natural as well as legal persons can be shareholders of a GmbH. Shareholders are not only entitled to many rights but they also have duties. The rights include the right to vote, the right to obtain information and the right to any surplus upon liquidation. The shareholders wield their power by approving resolutions during the General Meeting. Usually the shareholders receive one vote for every 50 Euro of the share capital they own. However, this can be differently directed by the Articles of Association.

All shareholders must be treated equally in order to ensure that no shareholder is subjected to unequal treatment or by the company or any other shareholder without his or her approval.

Another sharholder's right is the right to inspect the company's books and records and to be informed of the matters of the GmbH. Additionally, a shareholder has a claim to the profits stated in the annual financial statement unless the Articles of Association state otherwise. A shareholder's duty however includes locality not only to the company but also to other shareholders which limits the extent to which the shareholder can pursue his or her own interests.

- **Liabilities**

The GmbH's liability is limited to the amount of its registered share capital. Therefore, shareholders are not subject to any personal liability or obligations and piercing the corporate veil only takes place in very rare cases. (for example: fraudulent actions).

- **Accounting and Disclosure**

Every GmbH has to keep accounting records and prepare annual financial statements pursuant to the regulations of the German Commercial Code (Handelsgesetzbuch; HGB). These regulations lay down detailed requirements concerning the form and content of the statements. In addition to that, large and medium-sized companies must have an auditing for their annual financial statements. However, the statements must be lodged with the Commercial Register within twelve months of the end of each financial year.

- **Costs**

The formation of GmbH always involves costs. This is necessary in order to prevent the participants from inconsiderate behaviour. Therefore, the additional costs have a warning function. However, the costs depend on the share capital which means that the costs for formation are not fixed but vary from each individual formation to the other. In addition to that, the costs are higher for a GmbH that includes only one person (Ein-Personen-GmbH) than for a GmbH that consists of more people.

- **General overview of the GmbH's advantages**

In summary, a GmbH includes the following advantages for foreign investors:

First of all, a GmbH's formation is quite simple and does not include many difficulties. In addition to that, the Articles of Association can easily be adapted to the shareholders requirements and there are not as many legislative regulations concerning a GmbH as to other business entities (eg. AG or SE). And ultimately, the shareholders are able to influence the management directly due to the fact that they are entitled to issue binding instructions to the Managing Directors. Therefore, a GmbH is an easily formed and flexible business entity.

2. Mini-Limited Liabiltiy Corporation Company (Unternehmergesellschaft haftungsbeschränkt, UG)

As of November 01, 2008, German has established the so-called Mini-Limited Liabiltiy Corporation Company (Unternehmergesellschaft haftungsbeschränkt, UG) as a response to the UK Limited. The quintessential feature of the UG is the waiver of the traditional German minimum capital requirement. This is also the main demarcation line between the UG and the "regular" GmbH, for which the MoMiG retains the minimum capital requirement of 25.000 Euro.

Yet, the UG is not an entirely new form of company, but actually only a new kind of subtype of the well-tried GmbH. The UG is subject to the same rules and regulations which

are applicable to the “regular” GmbH. Thus, the UG will make it possible to “start small” and then gradually expand the business to a “full-grown” GmbH without the need for re-registration. But as long as the registered capital stays below the threshold value of 25.000 Euro for a GmbH, the UG must trade under the designation “Unternehmergesellschaft

(haftungsbeschränkt)” and must pay up the entire amount of the registered share capital before registration. In addition, a UG will be required to set up a reserve equal to a quarter of the annual surplus minus the accumulated deficit of the preceding year

3. Stock Company (Aktiengesellschaft, AG)

The AG is usually used by larger companies. This is also due to the fact that its legislation, the Stock Corporation Act (Aktiengesetz), provides less flexibility and most of its legislations are mandatory which can only be modified by the Articles of Association if this is explicitly permitted by the Stock Corporation Act. Therefore, an adaption to the shareholder’s requirements is not possible offhand. However, the advantage of an AG in comparison with a GmbH is the fact that shares can be transferred easily and the AG can be listed at a stock exchange and is therefore able to equity capital from the public.

- **Formation**

In order to form an AG one or more shareholders are needed. First of all a notarization of the Articles of Association is required. After that the founding shareholders must appoint the first Supervisory Board and the Statutory Auditor. These appointments must be notarised. The Supervisory Board then appoints the first management. Subsequently, the founding shareholders must prepare a written formation report, including all relevant details of the establishment of the AG. The Management Board and the Supervisory Board will then scrutinise the formation report. (In some cases an auditing of the formation report by an independent auditor might be required). Following this procedure the formation of the AG has to be registered with the Commercial Register. The application for registration has to be signed before a notary public and by all founding shareholders and the initial members of the Managing Board and the Supervisory Board.

- **Liability**

Upon registration stockholders are not personally liable to the AG. Instead of that, their duties are limited to paying the contributions owed. However, the AG only becomes a legal person on registration. People acting for and on behalf of the AG prior to registration will be liable for any debts incurred.

- **Share Capital and Shares**

The registered share capital must not be less than 50.000 Euro and is divided into shares. These shares can be par value or without a par value. However, the German law distinguishes even further between bearer shares (name of the owner is not registered) and registered shares (the name of the owner has been registered in the AG's share register). The Articles of Association must specify the types of shares that are issued. Bearer shares my not be issued until they are fully paid. Contributions to share capital can be either in cash or, if permitted by the Article of Association, in kind. In the latter case, contribution must be fully made upon registration. Shares are transferred easily within an AG. In comparison to a GmbH the transfer does not need a notarized transfer deed.

- **Articles of Association**

The minimum content of the Article of Association is determinated by the German Stock Corporation Act. It includes:

- The company's name and information about it' s registered seat
- Amount and division of the company's share capital
- Types of shares
- Number of the members of the Management board
- Object of the company

In addition to that, the Articles of Association may determine other aspects. However, it must be noted that this is only possible where it is explicit allowed by the German Stock Corporation Act.

- **Management Board**

The Management Board not only manages the AG but also represents it in and out of court. Contrary to the GmbH neither the shareholders nor the Supervisory Board is allowed to issue binding regulation to the Management Board concerning the AG's management. The members of the Management Board are appointed for a maximum term of five years. Furthermore, it is necessary that the members are stockholders. However, German nationality or residency is not required. The members are appointed by the Supervisory Board. AG's with a registered share capital of more than 3 million Euro must have a Management Board of at least two people (unless the Articles of Association states otherwise).

The members need to apply the standard of a prudent business person to their dealings. If they breach their duties the members of the Management Board are jointly and severally liable to the AG. In this context the burden of proof lies with members who must then proof that they complied with their duties. However, the Management Board is not liable if they can reasonably assume that they acted in the company's best interest.

- **Supervisory Board**

The Supervisory Board is the controlling body of the AG. Its main task is it to supervise and advise the Management Board. The Supervisory Board is appointed by a simple majority vote of the shareholders (unless the Articles of Association provide that a specific shareholder shall appoint one or more members of the supervisory board.) The members are appointed for a term of five years.

The main functions of a Supervisory Board are:

- the appointment and dismissal of the Members of the Management Board
- Representation of the AG's during its dealing with the Management Board
- Supervision of the Management Board
- Review and approval of the annual financial statements

- **General Meeting**

The shareholder's power is exercised by passing resolutions in General Meetings. During such meetings the shareholders appoint the members of the Supervisory Board and the auditors. The General Shareholders' Meeting also approves of the balance sheet profit and decides on amendments of the Articles of Association and on the handling of the company profits (dividend payment). A simple majority of the votes is usually enough for most corporate decisions. However, decisions involving major changes such as amendment of the Articles of Association must be taken by a qualified majority of at least three-fourths of the share capital represented at the meeting. In making their decisions the shareholders have a duty of loyalty to the company but not to other shareholders.

- **Accounting and Disclosure**

The AG has to keep financial records and must provide annual financial statements pursuant to the legislations of the German Commercial Code. In addition to that, medium sized and large corporations must have their annual financial statements audited. These

financial statements have to be handed in to Commercial Register within the twelve months of each financial year.

4. Partnership limited by shares (Kommanditgesellschaft auf Aktien, KGaA)

A KGaA is rarely used in Germany. It combines the structures of a limited partnership and an AG. A KGaA can be formed by setting up a new corporation or by converting an existing business entity into a KGaA. It is basically a limited partnership in which the partners receive shares instead of contributions. Besides this, the shareholders are organised in a way which is comparable to a Stock Company with a Shareholders' Meeting and Supervisory Board. Nevertheless, the shareholder's rights are not as extensive as those in a Stock Company. Furthermore, at least one general partner is needed, who then is personal liable for debts and liabilities of the KGaA. A partnership limited by shares has the same accounting and disclosure obligations like an AG. However, it should be taken in consideration that this rarely used business entity causes additional incorporation costs and higher costs for tax compliance. Consequently, a KGaA should only be considered as the appropriate business entity if the KGaA is the right form to achieve a preferred tax treatment or if investors shall be attracted but the control rights of shareholders comparable to an AG shall be avoided.

5. European Public Limited Company (Societas Europaea, SE)

The determinating provisions which regulate a SE are based on an EU regulation which got implemented by German law. The structure of a SE is quite similar to an AG. Every SE in Germany must have a link to at least two member states of the European Union. As a result of that, sheer German business operations can not be carried out through an SE.

Altogether, there are four possibilities in order to form a SE :

- at least two already existing corporations from different EU member states form a holding SE
- at least two already existing corporations from different EU member states form a joint subsidiary SE
- an already existing stock corporation (having a subsidiary in another member state for at least two years) is being converted into a SE

- Merger of two or more already existing stock corporations.

The SE must be registered with the Commercial Register with minimum share capital of 120.000 Euro. Shareholders are not subject to any personal liability for the SE and their duties are limited to paying the contributions owed. A SE in Germany can choose between two different ways of structure: It may either opt for the English single board system or the German dualistic system (management board and supervisory board). Therefore, a SE with its headquarters in Germany may opt for the English board system.

However, what is also special about a SE is the fact that it is entitled to relocate its principle place of management and its registered office to another EU member state. As a result of that, a SE provides high flexibility for future developments and allows companies to unify their structures across European boundaries. It is therefore especially suitable for businesses with operations in multiple EU countries.

6. Partnerships

There are two types of Partnerships:

- Limited partnership (Kommaditgesellschaft, KG)
- General Commercial Partnership (Offene Handelsgesellschaft, oHG)

The main difference between these two forms of partnerships is in the liability of its partners.

- General Commercial Partnership (Offene Handelsgesellschaft oHG)

An oHG is a typical business entity for small and medium sized companies.

Even though an oHG does not have a legal personality it is treated as an independent entity to the extent that it can acquire rights, enter into engagements and appear in court proceedings. In order to found an oHG two or more people have to conclude a partnership agreement (a one-man oHG is not permitted.) The oHG has to be registered with the Commercial Register and the local trade office. Furthermore, the General Commercial Partnership arises upon signing of the partnership agreement by the partners and start of business activity. As a result, its formation does not directly depend on the registration as such. All partners are jointly and severally liable for the oHG's debts and liabilities.

- Limited Partnership (Kommaditgesellschaft, KG)

The partners of a KG are divided into two groups: At least one partner (the General Manager) is liable personally without limit while the other limited partners are only liable with their registered partnership contribution. The formation process of a KG is quite similar to the one of an oHG: A partnership agreement hast to be concluded and the KG has to be registered with the Commercial Register. The KG exists legally with the signing of the partnership agreement unless otherwise provided. As a result, the legal existence occurs independently of the time of registration with the trade registry. In this context it is important to note that there indeed is a risk of a liability gap: the limited partners are fully and personally liable for all liabilities of the KG until it has been registered.

- GmbH & Co. KG

A GmbH & Co. KG is a special form of a limited partnership (KG) in which a corporation participates as a general partner. As a result of that, a GmbH & Co. KG is a partnership in which no natural person is liable for the KG's obligations. Since the GmbH & Co. KG basically consists of two companies (the Limited Partnership itself (KG) and the Limited Liability Company (GmbH)) its formation is governed by the regulations for the establishment of a GmbH and a KG. The GmbH as well as the KG have to be registered with the Commercial Register. As mentioned above the general partner is subject to unlimited liability for obligations of the KG. However, as the general partner is a GmbH, its liability is generally limited to its registered share capital. The limited partner on the contrary is only subject to liability with respect to its initial contribution in the KG.

The accounting and disclosure requirements for a GmbH & Co KG are close to those of a corporation. A GmbH & Co KG is therefore required to deposit its financial statements with the district court administering and the trade registry. Furthermore, the financial statements also have to the submitted to the electronically-maintained Federal Gazette.

- Limited & Co. KG / UG & Co. KG

A Limited & Co. KG/ UG & Co. KG is also a special form of a limited partnership, which is comparable to the GmbH & Co. KG. However, in this case a UK-based Limited / a UG participates as general partner. In the event of a Limited & Co. KG / UG & Co. KG being formed no natural person is liable for the KG's obligations.

7. The Advantages of a Partnership compared to a corporate structure

The following points are usually invoked concerning the advantages of a partnership and should therefore be taken into consideration when choosing a specific form of business entity.

A partnership distinguishes itself due to:

- the direct management by the general partners
- the fewer publication requirements
- the easy way of dissolving a partnership and distributing its capital to the partners
- the greater flexibility in adapting the internal affairs to the partner's needs.
- beneficial gift and tax treatment

8. Other

- Branch

Carrying on business in Germany by registering as a branch is especially suitable for companies not yet sure about the sustainability of their commitment in Germany. The branch has to be registered with the Commercial Register and the Trade office.

However, a branch has no legal entity status within Germany. This leads to the result that the branch is regarded as an integral part of a foreign company. The foreign company is therefore still liable for all commitments and debts arising from the branch's business operations. Nevertheless, it must be taken in consideration that a branch establishes jurisdiction for the respective company in Germany.

- Sole Tradership

Especially for individuals the sole trader (Einzelkaufmann) represents the easiest way of starting a business in Germany. The registration with the Commercial Register and a notification to the local trade office (Gewerbeamt) are the only requirements for starting such a business (unless a special regulated business is carried out). However, in some industries special approvals and permissions are compulsory. Furthermore, the sole trader is also the sole proprietor of all assets. He or she is therefore personally liable for all liabilities and debts arising from the business.

G. Taxation

1. General information

Germany does not provide one consistent nationwide tax rate for all companies. Instead of that, it has to be distinguished between corporations (such as the GmbH and AG) which are subject to corporate income tax (Körperschaftssteuer) and partnerships which are subject to personal income tax (Einkommenssteuer). Both of these taxes are levied by the German government. In addition to that, all German business operations (corporations and partnerships) are subject to the trade tax (Gewerbesteuer). This tax is levied by local municipals such as the city where the company is based.

2. Corporate Income Tax

Corporate companies based in Germany or with an executive board in Germany are not only subject to German income tax on the profits they make in Germany but also on their worldwide generated income. However, other corporate companies are only liable to income tax on the income generated inside Germany.

The tax base for Corporate Income Tax is formed by the taxable income (annual business profit). In Germany this is being calculated according to accrual basis accounting method which is recorded in the annual financial statement.

The Corporate Income Tax rate currently amounts to 15 % of the taxable income. In addition, a Solidarity Surcharge is added on top of this Corporate Income Tax. This solidarity surcharge is 5.5 % of the 15 % corporate income; creating a total of 0.825 % of taxable income. As a result, Corporate Income Tax and Solidarity Surcharge add up to a total of 15.825 %.

3. Personal Income Tax

Partnerships are associations of partners. Therefore the partners themselves are subject to all rights and obligations. Consequently, the tax rate is applicable to the individual income of the shareholders. Currently, the Personal Income Tax adds up to 14 % (2014) for an annual income exceeding the tax-free allowance of 8.354 Euro. Depending on the respective income it can however rise to a maximum income tax rate of 42 % which is applicable to an annual income of 52.882 Euro or more. Furthermore a tax rate of 45 % is applicable in excess of earnings of 250.731 Euro per year.

In addition, the Solidarity Surcharge which amounts to 5.5 % of the individual income tax rate of every partner is also added to Personal Income Tax (This means if an individual income rate is 30 % the total amount of tax will be 31.65 % of the individual income.)

4. Trade Tax

The Trade Tax has to be paid by all commercial business operations in Germany regardless of the legal form. Due to the fact, that the Trade Tax Rate is set by local authorities it can vary from one German location to another. However, the Trade Tax Rate generally varies between 7 and 17 %. Nevertheless, partnerships have an annual tax free allowance for trade tax of 24.500 Euro. The Solidarity Surcharge is not added to the Trade Tax Rate.

H. German Labour Law

The German labour and employment law is based on a variety of labour and employment acts. There is no unified German labour and employment act. The German Civil Code (Bürgerliches Gesetzbuch – BGB) contains general rules for labour and employment relationships, which are complemented and specified by numerous acts providing regulations for particular situations, for example:

- Protection Against Unjust Dismissals Acts (Kündigungsschutzgesetz - KSchG)
- General Equal Treatment Act (Allgemeines Gleichbehandlungsgsetz - AGG)
- Social Security Code (Sozialgesetzbuch – SGB)
- Maternity Protection Act (Mutterschutzgesetz – MuSchG)
- Part-Time and Limited Term Employment Act (Teilzeitbefristungsgesetz – TzBfG)
- Federal Paid Leave Act (Bundesurlaubsgesetz – BurlG)
- Working Time Act (Arbeitszeitgesetz – ArbZG)

Labour disputes are settled in front of a labour court. The Labour Court Act (Arbeitsgerichtsgesetz – ArbGG) regulates the labour law suits, including all disputes between employers and employees and also trade union disputes.

As Germany is a member of the European Union, labour law is strongly influenced by EU legislation and case law as well.

1. Collective agreements

In some branches, there are also collective labour agreements (Tarifvereinbarungen), based on the Act on Collective Agreements (Tarifvertragsgesetz – TVG). These collective agreements are concluded between Unions of the employees and employer's associations and are usually only binding for the contracting parties. Though, non-member parties can refer to a collective agreement. However, it is possible, that collective agreements are binding all employees of a branch, regardless of whether the employees or employers are a member of the Union (so called: branch- level collective agreement/allgemeinverbindlicher Tarifvertrag). There are for example branch- level collective agreements for the branches of catering industry, hotel business and construction. These collective agreements normally contain terms of paying, working conditions and working hours. They apply automatically to the employment contract. Therefore notwithstanding regulations are hardly possible.

2. Workers council

In companies with at least five employees, the Work Constitution Act (Betriebsverfassungsgesetz – BetrVG) authorizes the employees to elect workers council (Betriebsrat). The workers council is representing the needs and interests of the employees. Therefore it negotiates and agrees with the employer on so called agreements of work (Betriebsvereinbarungen). These often contain modalities of participation of the workers council, on termination and working hours. Agreements of work are binding the employer but are only applicable for the employees within the establishment. Workers council also need to be involved in case of giving notice to an employee, though its decision is not binding for the employer.

3. Principle of Equal Treatment

As the employer is obliged by the General Equal Treatment Act to treat all employees the same way, the latter do have a right of the same treatment if they are treated unequally and there is no objective reason for that.

4. Employment Contract

The written employment contract between the employee and the employer must contain the key aspects of the employment relationship, such as contracting parties, work to perform, gross salary and benefits, vacation, starting date of employment, notice periods, extra hours. If the employer will be represented for example by a human resources manager, it is recommendable for the employer to point that out to the employee and

that the representative is entitled to take measures against the employee, such as termination.

Even though if the employment treaty turns out to be reviewable or invalid but is administered (employee starts working), there will be a so called factual employment contract (faktisches Arbeitsverhältnis) with the content of the originally intended as far as valid. As a consequence the employer is obliged to pay salary and the employee to work.

4.1 Interview

If the employer advertises a job, he has to make sure that no discriminations are contained within. Otherwise there is the possibility of compensation and indemnity (§ 15 of the General Equal Treatment Act). In case of a personal job interview the employer has to be aware of that only questions related to the job function are allowed. Therefore, questions on health situation and previous convictions can be permissible. Also permissible is the question for disability because this leads to legal consequences for the employer. If permissible questions are answered wrongly, the employment contract is appealable or can be terminated. However, the employee has the right to avoid answering impermissible question and also is not obliged to answering them truthfully.

4.2 Employment Contract Contents

4.2.1 General Business Terms

Usually the employer dedicates the terms and conditions of the work contract to a large numbers of employees without negotiating them with the employee (so called: Allgemeine Geschäftsbedingungen). Because of the weak position of the employee the German law provides regulations (§§ 305 ff. German Civil Code (BGB)) which are protecting the employee. If there are passages in the employment contract which are not permissible by German law, they are deemed invalid but usually the rest of the contract remains valid. Furthermore, clauses are invalid if there are unclear.

4.2.2 Working Hours

German employees normally work from Monday to Friday (five-day-week). Saturday and holidays are none working days. The average working under a five day week time is between 35 and 40 hours, the daily productive working time may not exceed eight hours (breaks not included). However, it is possible to exceed the daily working time up to ten hours over a period of six months as far as the average daily working time does not exceed eight hours. Working on Sundays and public holidays is generally prohibited, but there are several exceptions in the Working Time Act (Arbeitszeitgesetz – ArbZG). There

are special regulations for female (MuSchG) and underaged workers (Young Worker Protection Act – Jugendarbeitsschutzgesetz – JarbSchG).

4.2.3 Probationary Time

The contracting parties often agree on a probationary time up to six months. During this period both, the employee and the employer can terminate the contract with a notice period of only two weeks (§ 622 Abs. 3 BGB).

4.2.4 Limited-Term

The requirements for limited-term employment contracts are covered by the Act on Part-Time and Limited Term Employment Act (Teilzeit- und Befristungsgesetz TzBfG). Generally limited term employment contracts are only permissible in writing and in case of an objective reason for the limitation, such as the temporary replacement in case of pregnancy, parental leave or illness. Without any grounds a limited-term contract is permissible for a maximum period of two years (or four limited-term contracts altogether not longer than two years). However, the contract may not follow any other contract with the same employer. It is also permissible if the employee is at the age of 52 years or more. If the employee claims the ineffectiveness of a limitation he/she enters into an unlimited employment contract.

4.2.5 Part.Time

The Act on Part-Time and Limited-term Employment Relationship provides also rules for part-time work. Part-time work describes an employee who works fewer hours than the weekly hours worked by full-time workers, which is in Germany between 35 to 40 hours in a 5-day-week. After working as a full-time employee for at least six months, every employee can request to work part-time (§ 8 TzBfG). The employer can only deny the request if he has to fear bad impacts on his company. A part-time worker who wants to work full-time must be given preference in case of a vacant full-time post.

4.2.6 Salary

Generally the contracting parties are free in the negotiation of the salary if there are no collective agreements. However, the law changed in Germany: from January 1st 2015 there will be a minimum wage in Germany at the level of 8.50 Euro per hour. This minimum wage affects almost every industry. Collective agreements containing a minimum wage below that level can only subsist until the end of the year 2016.

The Working Time Act (Arbeitszeitengesetz – ArbZG) contains provisions for the regulation of overtime, night and holiday working.

Additional payments such as Christmas benefits are not required by law. Often collective agreements provide for such payments, though. If the employer is not obliged to such payments, he needs to be aware of that a duty can arise because of customary law.

4.2.7 Paid Leave

The Federal Paid Leave Act (Bundesurlaubsgesetz – BUrlG) guarantees at least 20 days paid vacation per calendar year to the employees who work a five day week. However, it is common for an employee to receive between 25 and 30 days of vacation. There are special regulations for disabled and adolescents who receive longer vacation entitlements.

The full vacation entitlement requires that the employee has been working at least for six months. Before the expiration of the six months period, he/she will only receive proportional vacation.

If there are objective reasons, the employer can refuse the employees right to take his vacation as a whole. He/She also has to choose in respect of social criteria if several employees request vacation for the same time.

Generally, vacation has to be taken for the current calendar year. If it's not possible for the employee to take all his/her vacation, he/she is allowed to transfer it into the following year when he/she meets the legal requirements (§ 7 BUrlG). As far as German law determines, that after a period of three months of the next year the vacation of the preceding year expires this is not corresponding with the EU law. However, an expiry after 15 months is in accordance with EU law.

After terminating the employment relationships the right of vacation can turn into compensation if the legal requirements are met (§ 7 BUrlG).

4.2.8 Sick Leave

§ 3 of the Continuation of Remuneration Act (Entgeltfortzahlungsgesetz – EFZG) statutes, that in case of illness the employer has to continue payment of full salary for a period of six weeks, and under certain circumstances up to twelve weeks. Afterwards the health insurance makes sick payment (§ 48 V SGB V). The EFZG is only applicable if the employee has been working for four weeks.

4.2.9 Industrial Accident

When it comes to interior industrial accidents, there is a particular liability scale in Germany. If the accident is caused by an employee, the employer can be liable for the dam-

ages. This is because the employee usually has a much lower income and also the employer is benefiting much more and bears a less risk. In case of intentionally damages of course, the employee himself/herself is responsible and has to recompense the loss of the employer.

4.2.10 Maternity Leave

Female employees are entitled to full paid maternity leave. The maternity leave normally starts six weeks before the expected due date and ending eight weeks after childbirth. Afterwards part-time working can be requested. The payments are made partly by the statutory health insurance provider and partly by the employer. During pregnancy and maternity leave there is also a special dismissal protection.

4.2.11 Parental Leave

Parental leave is regulated in the Federal Act on Payment of Child Rising Benefit and Child Rising Leave (Bundeselterngeld- und Elternzeitgesetz). Both parents can take parental leave up to three years, but not at the same time. During this period the employer is not obliged to make any payments, but also not to terminate the employee. Employees are allowed to work part-time (up to 30 hours a week) during parental leave. If they want to work for a third party agreement of the employer is needed. Parents must give notice to the employer that they will be on parental leave at least six weeks before. During parental leave there is a particular dismissal protection.

4.3 Termination of Employment

4.3.1 Limited-Term Employment Contract

A limited-term contract ends automatically by expiration of the term. There is no termination notice needed and it is also not permissible if the contracting parties haven't agreed on it.

4.3.2 Dismissal with the Option of Altered Conditions of Employment (Änderungskündigung)

There is the possibility of a dismissal with the option of altered employment conditions. Here the employer terminates the existing employment contract and simultaneously makes an offer for a new employment contract with altered conditions. However, such dismissal is not admissible to reduce the salary of the employee only.

4.3.3 Cancellation Agreement (Aufhebungsvertrag)

Also common is a cancellation agreement (Aufhebungsvertrag). Here the employer and employee make a (written) contract about the ending of the existing empoloyment con-

tract. Advantages of this way of ending an employment contract is that no period of termination has to be considered and the employee is usually not causing any further problems (employment lawsuits). However, in most cases the employee is not entitled to unemployment benefits for twelve weeks as he is reliable for his unemployment by signing a cancellation agreement. Therefore employers offer sufficient financial compensation or other benefits.

4.3.4 Termination of the Employment Contract by giving Notice

Both, the employee and the employer do have the right of terminating the employment contract, but the latter has to meet higher legal requirements in case of unilateral termination. There are two kinds of termination in German labour law: ordinary and extraordinary termination. In both cases a written notice of termination is necessary (§ 623 BGB). Verbal notices are invalid and have to be redone. If a notice is given by a representative of the employer, he/she has to assure that proof of power for this measure is presented to the employee.

An ordinary termination leads to the ending of the employment relationship after the applicable notice period expires. The notice period is determined by law (§ 622 BGB) and takes at least four weeks and may be up to seven months, depending upon the length of the employment. The employer and the employee can agree on a longer notice period, however, a shorter period is invalid. If there is a worker´s council the employer has to consult it before giving notice of termination to the employee. However, the work´s council opinion is not binding (§ 102 BetrVG). Termination without proper hearing of the works council is invalid.

There is no notice period to be obtained in case of an extraordinary termination (§ 626 BGB). The employment relationship ends immediately. For an extraordinary termination serious reasons are needed which make it, in good faith, unacceptable to continue the employment relationship until the end of the notice period. It is only permissible within 14 days after knowledge of the facts of the serious reason.

If a labour court holds a termination notice invalid, the employer must pay the employee´s salary for the entire duration of the proceedings. Furthermore, the employer is obliged to reemploy the employee.

4.3.5 General dismissal protection

As the German labour law tends to protect the employee, there are various regulations dealing with dismissal protection.

General dismissal protection is provided mainly by the Protection Against Unjust Dismissals Act (Kündigungsschutzgesetz – KSchG). If applicable, ordinary termination is only legitimate if the requirements are met (§ 1 KSchG). The Protection Against Unjust Dismissals Act is applicable to employees working in a company for more than six months and which has employed more than 10 employees (apprentices do not count). If the act is applicable, the employee may only be terminated for three particular reasons which are enumerated in the act. These are operational reasons (betriebsbedingt), behavioural reasons (verhaltensbedingt) and reasons which are not based on a bad behaviour but the person (personenbedingt). No matter of which reason the employee is noticed, the employer always needs to prove the reason. He also has to prove in case of an operational notice, that there is no other possibility, e.g. another comparable job within the company plus that he regarded social criteria (age, seniority, family reasons, disability). In case of behavioural reasons, normally a warning letter (Abmahnung) is necessary before giving notice to an employee; otherwise the termination notice is unfair. If a dismissal follows a warning letter, both have to base on the same misconduct.

4.3.6 Particular Dismissal Protection

Besides that, there is particular dismissal protection against ordinary and extraordinary dismissal for some groups of employees due to their individual circumstances. This includes for example pregnant women, (§ 9 MutSchG), heavily disabled (§ 85 SGB IX) and members of worker´s council (§ 103 BetrVG, § 15 KSchG). In these cases, prior approval of various German authorities is required for the termination of employment, which is usually very difficult to obtain.

4.3.7 Employment Reference Letter

After the ending of the employment relationship the employer is also obliged to draw up an employment reference letter in which he/she has to describe and appreciate the work of the employee and the employee himself. In case of legitimate interest, the employee is entitled to ask for such a letter during the existing employment contract (so called interim performance report).

5. Labour Law Suits

The Labour Court Act (Arbeitsgerichtsgesetz – ArbGG) establishes special labour courts, consisting of three instances: the Labour Court, the State Labour court and the Federal Labour Court. The jurisdiction of the labour courts covers most issues with labour references (§ 2 ArbGG)

There are some specifics about labour law cases compared to normal civil suits. As usually, the party who loses the case has to pay the court fees and the legal expenses also of the winning party. This is different in labour cases: in the first level each party has to pay its own lawyer - regardless of which party wins or loses.

There are also very short periods for filing suits. For example in case of the validity of dismissals, there is only a three-week period for filing the dismissal suit (§ 4 KSchG).

6. Taxes and Social Insurance Contributions

Employees pay income tax on their income. Rates are between 15% and 42%. The employer has to forward the income tax to the tax authorities. Any tax deductions have to be made together with the employee's tax declaration.

The social security system is regulated by the Social Security Code (Sozialgesetzbuch – SGB). The mandatory Social Security System in Germany consists of health insurance, home care and nursing insurance, pension insurance and unemployment insurance. The premiums are paid half by the employers and half by the employees. The employer has to pay dues to approximately 20% to 22% of the employee's gross salary, depending on the employee's tax category.

7. Ostensible Self-Employment (Scheinselbständigkeit)

There is no obligation for such social security contributions for freelance workers who are self-employed and therefore responsible for themselves. A freelance worker is someone who is not bound by instruction. He is making his own decisions freely and bears his own entrepreneurial risk. In general he is working on his own behalf and expense. Also the provisions for dismissal protection do not apply.

If someone is ostensible self-employer, he is appears to be a freelance worker, but in fact he is an employee.

The distinction between self-employment and ostensible self-employment isn't always easy. The latter is assumed if the "self-employee" is working only for one principal and generates the large part of his revenue out of this work. Further it is influential whether

the performed work is typical work for an employee or if entrepreneurial thinking and decisions are necessary. Eventually, this distinction is a matter of the individual case (§ 7 SGB IV). Problems can occur for the principal, if the freelance worker turns out to be an ostensible self-employee. This leads to the employers duty to pay social insurance contributions in arrears for a period up to four years as the principal employed an employee. Additionally, fines can be imposed too. Furthermore, the ostensible self-employee is entitled to claim for a employment contract including dismissal protection, paid vacation and paid illness.

Because of the legal consequences of a wrong classification, there is the possibility of performing a “procedure of qualification” (Statusfeststellungsverfahren) at the Clearingstelle für sozialversicherungsrechtliche Statusfragen, 10704 Berlin, which is an institution by the German Pension Insurance.

Tiefenbacher
ATTORNEYS | TAX ADVISERS

Im Breitspiel 9
69126 Heidelberg
Germany
Tel. +49 (0)6221 3113.0
international@tiefenbacher.de

Key contacts:

Dr. Gero Schneider M.C.L.
g.schneider@tiefenbacher.de

Marcello Di Stefano
distefano@tiefenbacher.de