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LIABILITY OF PRINCIPAL CONTRACTORS:

SELECTED NATIONAL EXPERIENCES

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Executive summary

The EU Directive on the Posting of Workers (Directive 96/71/EC) states that workers posted by an employer to perform work in another EU member state should be guaranteed the minimum provisions laid down by law or collective agreement in the host country. However, market evidence suggests that chain subcontracting can obscure the link between the principal employer and the employee, thus jeopardising the application of provisions aimed at protecting posted workers. As a matter of fact, by creating extremely complex networks of sub-contractors, main contractors can often create an easy way to circumvent legal or collectively agreed labour standards and working conditions. Nowhere is this as relevant as in the construction sector.

In order to tackle this problem, many European countries have made the chief contractor of a chain legally responsible for compliance with regulations, including labour laws and tax laws, by subcontractors. These measures are commonly referred to as "client liability" or "chain liability", or also "joint and several liability" of main contractors. Such liability schemes were considered to be restrictions compatible with the freedom to provide services in a recent judgment by the European Court of Justice, *Wolff & Müller v José Filipe Pereira Félix*, related to the German joint and several liability rule.

This briefing note illustrates in detail client liability rules enacted in Austria, France, Germany, Ireland, The Netherlands, Portugal, Spain and UK, and provides some basic information on new member states. All other surveyed countries but UK and Ireland apply systems of joint and several liability, which however differ among themselves in many respects:

- In some cases (Germany, Spain and the Netherlands) national law allows workers to claim directly and immediately against the main contractor; in others (Austria), the general contractor cannot be held liable until redress has first been sought against the actual employer.
- Some countries apply chain liability only in specific sectors (i.e., the Netherlands, for the construction and clothing sectors).
- Some countries introduced rules only for the protection of temporary agency workers (Portugal).
- The nature and purpose of the liability differs, as in some countries – e.g., Austria – liability exists towards social security and tax authorities, whereas in other countries client liability aims at securing the protection of workers' rights.
- The legal consequences of client liability differ amongst surveyed countries: on the one hand, in Germany, Austria and the Netherlands liability includes the imposition of fines. Conversely, in France no financial penalty is imposed on main contractors, which only have an obligation of vigilance over subcontractors.

As regards new member states, most of them have recently amended their Labour Codes to introduce protective measures for posted workers, but only two of them (Hungary and Slovenia) are considering the introduction of client liability rules.

LIABILITY OF PRINCIPAL CONTRACTORS:
SELECTED NATIONAL EXPERIENCES

Introduction

Over the past few years, the cross-border provision of services in many EU industry sectors has increasingly taken the form of subcontracting and agency work. Firms established in an EU Member State often use subcontractors based in other Member States to carry out part of the services to be provided. This trend is visible especially in some industry sectors, such as the construction industry. By creating extremely complex networks of sub-contractors, main contractors can often create an easy way to circumvent legal or collectively agreed labour standards and working conditions. In most EU countries, provisions on posted and temporary workers have been too easy to circumvent through this practice. This, in turn, created the concern on a possible "race to the bottom", in which firms exposed to price competition by firms using cross-border chains of low-cost subcontractors have no almost choice but to elude national labour and working conditions laws in order to survive on the market.

The EU Directive on the Posting of Workers states that workers posted by an employer to perform work in another EU state should be guaranteed the minimum provisions laid down by law or collective agreement in the host country. However, chain subcontracting can obscure the link between the principal employer and the employee. At the bottom of the chain, recipients may be declared as self-employed and then escape taxation on earnings. Also, individuals who are declared as employees of a very small enterprise may claim to have already had social security contributions and tax deducted from their pay, while the very small enterprise has disappeared without handing the money over to the tax authorities. In addition, subcontractors can more easily evade some of their taxes and social security contributions, by over-reporting material costs and underreporting their own wage costs.

Many European countries have made the chief contractor of a chain legally responsible for compliance with regulations, including labour laws and tax laws, by subcontractors. These measures are commonly referred to as "client liability" or "chain liability measures", or also "joint and several liability" of main contractors. In several occasions, the European Parliament and some social partners endorsed the principle of general or principal contractors having joint and several liability for subcontractors' obligations towards their workers, taking the view that this reinforces the liability of contractors to monitor compliance with the employment legislation by their commercial partners.

This briefing note describes some national experiences of EU member states as regards the imposition of client liability for the case of non-compliance with employment legislation by their subcontractors and/or employment agencies. To this end, we will refer exclusively to civil liability rules aimed at ensuring compliance by subcontractors with obligations towards their workers and/or the tax and social security authorities. In addition, preference will be given to rules aimed at tackling the problem of illegal foreign workers and temporary agency workers in the provision of cross-border services. Section 1 describes national experiences in imposing joint and several liability for subcontractors, with focus on Austria, France, Germany, Ireland, The Netherlands, Portugal, Spain and UK. Section 2 briefly describe the rules applicable in Accession countries, whereas Section 3 concludes. Appendixes B and C describe two important cases decided by the European Court of Justice and the UK High Court.

1 Selected National Experiences

Client liability schemes are currently applied in a number of member states, including Austria, France, Germany, the Netherlands, Portugal and Spain[1]. However, the schemes currently in place – some of which have been introduced or revised in the transposition of the Posting of Workers Directive – differ in many respects. Below, we briefly illustrate the main features of such national rules.

1.1 Austria

In Austria, already before the transposition of Directive 96/71/EC, the posting of workers had been legally regulated in 1993 with the *Arbeitsvertragsrechts-Anpassungsgesetz* (AVRAG)[2]. According to this act, employees posted to Austria for longer than one month had the right to claim the collectively agreed wage of the working site. The aim was to apply the work and social legal standards of the working site for jobs in Austria provided that they lasted a certain time. Two years later, the Anti Abuse Act (*Antimissbrauchsgesetz*) of 1995 abolished the one month limit and introduced a joint and several liability of the foreign employer and his Austrian customer for wage claims of the posted employees. At the same time, the employer is obliged to keep at the place of work all documents necessary to determine the wage as well as documents on the registration of the employee for social security in the country of origin.

In order to protect those employees, who have their usual work place in Austria, whenever their employers are not based in Austria nor participate to a corporation empowered to engage in collective bargaining negotiations, new rules were then introduced by Section 7 of the Employment Contract Adjustment Act, which transposed Directive 96/71/EC on the Posting of Workers Directive[3]. According to Section 7, these employees must be entitled, as a minimum, to the remuneration – laid down by law, ordinance or collective agreement – that is due to comparable employees of comparable employers at their workplace[4]. To the contrary, the system of paid leave funds for construction workers is not applicable to workers posted from abroad.

The main features of the Austrian rule are: *a)* The *chain liability of general contractors*: any undertaking whose subcontractors fall foul of the law governing public tenders or public contracts is deemed liable for the pay of the workers employed by the subcontractor; *b) Secondary liability*: the general contractor cannot be held liable until redress has first been sought against the actual employer; and *c) Performance guarantee in the construction sector*: in the event of legal subcontracting in the building sector, the principal undertaking must furnish a performance guarantee as regards the pay claims of the workers against the subcontractor.

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[1] Similar rules are in force also in Belgium, Denmark, Italy and Sweden.

[2] Federal Act to conform with regulations concerning employment contracts and to amend the Acts regarding employees and domestic servants to EU law (*Arbeitsvertragsrechts-Anpassungsgesetz*, BGBl. 1993/459).

[3] In 1999, both the Temporary Work Act (*Arbeitskräfteüberlassungsgesetz*, AÜG) and the Employment Contract Law Adaptation Act (*Arbeitsvertragsrechts-Anpassungsgesetz*, AVRAG) were amended due to the requirement to implement the EU Directive.

[4] Austrian legislation concerns cross-border postings carried out by foreign employers (established in a country other than Austria). The interpretation of the legal rules governing posting, reinforced by Austrian private international law, suggests that posting corresponds to temporary transfer of the workplace, which is normally located in the worker's country of origin. The ECJ in *Rush Portuguesa* gave equal status to legislation and collective agreements. See Case C-113/89, 27 March 1990.

1.2 *France*

In France, a rule establishing the obligations of main contractors for failure of subcontractors to perform their contractual obligations vis-à-vis their employers entered into force already in 1979, under Article L-124.8 of the Code du Travail (Labour Code), introduced by Law n. 79-8. This rule is specifically referred to entrepreneurs posting temporary workers (*entrepreneur de travail temporaire*), defined as "all physical or legal entities whose exclusive activity is to place at the temporary disposal of clients workers of an agreed qualification that they pay in light of these activities". According to Article L-124.8, employers posting temporary workers must always keep a financial guarantee to ensure, in case of its failure to perform contractual obligations, the payment of wages and indemnities and the payment of social security. If this guarantee is found to be insufficient, the customer will be liable for the remaining obligations, *in lieu* of their subcontractor, both vis-a-vis their subcontractors' employers and towards social security administrations.

Joint and several liability was introduced only a few years later, in 1997. Since the enactment of the Act of 11 May 1997, French law provides that the final recipient of a service, i.e. the customer or main contractor, can be held liable for the financial consequences of illegal employment by suppliers or subcontractors. He can thus be required to pay the pay-roll costs, including social charges and tax, left unpaid by the direct employer, under the rule of "financial solidarity" between co-contractors. The customer or main contractor may escape liability, however, if he can prove that he monitored the co-contractor's compliance with rules on the employment of foreigners.

Under the 1997 Act, anyone (individuals excepted) who upon signing a contract does not receive confirmation that the other party to the contract is in compliance with the rules regarding employment of foreigners, also becomes jointly and severally liable for the special contribution to the *Office des migrations internationales* (OMI), which applies to any contract with a value of FRF 20,000 or more. As a result, an employer who hires a foreigner without a work permit and does not report the hiring to the social welfare authorities, immediately incurs two violations: employment of an undocumented foreigner and concealment of an employee. Prosecution of these two offences thus brings the aspect of joint and several liability into play twice against the principal, inasmuch as the detriment incurred and the claimants on these respective offences are different. According to Marie (2000), the first few judgments brought against principal contractors in application of joint and several liability have had a positive effect on industry players' behaviour.

As regards the French construction sector, in 1995 six professional organisations in the building industry and civil engineering adopted a new standard contract for subcontracting. This contract includes a provision requiring the company that subcontracts to make sure when concluding a contract that the subcontractor exercises the activity within regular conditions, excluding all kinds of undeclared work.

1.3 Germany

In Germany, the Act on the posting of workers (*Arbeitnehmerentsendegesetz,* AEntG) and the Act that regulates the professional temporary employment *(Arbeitnehmerüberlassungsgesetz)* entered into force in 1997[5]. The AEntG introduced the following rules:

- *registration obligations* for posting companies;

[5] Act on labour conditions in the case of cross-border services *Arbeitnehmerentsendegesetz*) and the Act that regulates the professional temporary employment *(Arbeitnehmerüberlassungsgesetz)* (§ 5 AEntG; §§ 15, 15a, 16 AÜG).

- *Sanctions*: infringement of the AEntG (and in particular, to the provisions on minimum wage, holidays and holiday pay, and registration and cooperation obligations) is treated as an administrative offence, leading to fines and the exclusion from the award of public contracts. Priority is given to punishing the company committing the offence, but the client can also be punished if it knows, or is negligent in not knowing, that a subcontractor employed by it is not complying with the minimum working conditions. Fines up to one million DM (€500,000) may be imposed[6];
- *General contractor liability*: clients are directly liable if their subcontractors (and also the latter's own subcontractors) do not pay their employees the minimum wage or do not pay the construction industry's holiday fund the contribution to which it is entitled. In other words, it is part of the general contractor's duty of care to select subcontractors (*culpa in eligendo*) and to monitor their compliance with relevant provisions of the AEntG (*culpa in vigilando*).

This provision was later amended in 1999: the scope for penalties was increased, and the general contractor liability was made independent of a finding of negligence. In other words, the general contractor today has strict liability in the event that a sub-contractor does not pay the minimum wage stipulated under the AEntG or does not pay over contributions to the construction industry's holiday fund. Under Section 1(a) of the AEntG, as in force since 1 January 1999, the main contractor "is liable for the obligations of that undertaking, of any subcontractor and of any hirer of labour appointed by that undertaking or subcontractor concerning payment of the minimum wage to a worker or payment of contributions to a communal scheme for parties to a collective agreement ... The minimum wage for the purposes of the first sentence, means the sum payable to the worker after deductions in respect of tax, social security contributions, payments towards the promotion of employment or other such social insurance payments (net pay)."

In other words, the principal contractor is considered to be in the position of a guarantor who has waived the benefit of execution (*beneficium ordinis*). The wage liability covers the whole chain of subcontracting, but only with regard to net pay, not extended to social security, taxes etc. According to some commentators, the German rule on general contractor liability has not exerted a major impact as a result of generous allocation of certificates of exemption. In addition, liability for social security contributions has lost much of its effectiveness by being limited to the first sub-contractor.

As regards the construction sector, from 2002 Germany introduced the principle of general contractor liability for the social security contributions of the workers of a subcontracted firm[7]. Due to this modification it will be in the interest of an entrepreneur to verify whether or not their subcontractors take on illegal workers.

1.4 Ireland

In Ireland, no distinction is made in employment rights legislation as between Irish and migrant workers. Section 20 of the Protection of Employees (Part-Time) Work Act 2001 provides that all employee protection legislation on the Statute Book in Ireland applies to workers posted to work in Ireland in line with Directive 96/71/EC on the Posting of workers. Thus, all employee legislation also applies to migrant workers. Equally, the Labour Inspectorate and the compliance section as a whole of the Department of Enterprise Trade and Employment makes no distinction as between Irish and migrant workers both as regards the provision of advice and enforcement activity.

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[6] Fines for the foreign employee are much lower, amounting to 5,000 Euro for working without work permit.

[7] *Gesetz zur Erleichterung der Bekämpfung von illegaler Beschäftigung und Schwarzarbeit* (Act on the Simplification of the Fight against Illegal Employment and Moonlighting), 23.7.2002, published in BGBl I 2002 Nr. 52, 29 July 2002.

In Ireland, no client liability rules has been introduced for tackling "triangular" cases of subcontractors or employment agencies failing to comply with relevant employment legislation. The lack of specific rules on client liability is of particular importance when it comes to protecting the rights of temporary workers. As there is no comprehensive labour code in Ireland, the employment conditions of temporary workers are covered in both statute law and case law, leading to a somewhat confusing legal framework.

In the mid-eighties a decision taken under Irish case law deemed that the "agency temp" is not an employee of the hiring company and thus does not have any protection under the legislation[8]. However, the inclusion of a provision in the Unfair Dismissals (Amendment) Act of 1993, reversed this decision. The 1993 Act provides that the party hiring the individual from the employment agency is deemed to be the employer, whether or not this third party pays the wages in respect of the work or service[9]. Under the Act, temporary agency workers shall be entitled to bring unfair dismissal claims for redress against the hiring company that is the employer with whom they are placed, provided they meet the necessary service qualifications. Whereas under the Unfair Dismissals (Amendment) Act, 1993, the employer is the person for whom the agency works, in other pieces of legislation – *e.g.*, the Terms of Employment (Information) Act, 1994, the Maternity Protection Act, 1994, and Organisation of Working Time Act, 1997 – the person who pays the wages is considered to be the employer of the agency worker.

The Organisation of Working Time Act, 1997, sets out statutory rights for employees in respect of rest, maximum working time and holidays. Holiday pay is earned against time worked. There is no qualifying period for holidays and all employees regardless of status or service qualify for paid holidays. Legislation on working time also concerns temporary work. In the case of agency workers, the person who is liable to pay the wages (employment agency or hiring company) is the employer for the purposes of the Act and is responsible for providing the holidays/public holiday entitlement.

1.5 The Netherlands

In the Netherlands, chain liability was introduced already in 1982 in the construction sector, with the Chain Liability Act. The *Wet Ketenaansprakelijkheid* (Law on ultimate responsibility for certain payments) of 4 June 1981 inserted new provisions in the *Cooerdinatiewet Sociale Verzekering* (CwSV) of 24 December 1953 (Law on the coordination of social security provisions with the provisions on the taxation of wages and salaries)[10]. These new rules were enacted for the purpose of combating dubious subcontracting practices by main contractors wishing to circumvent the fiscal laws.

The Chain Liability Act stipulates that the main constructor is holding responsibility for the payment of taxes and fringe benefits by the subcontractors. This Act was reviewed and subsequently refined in 1991. Under Article 16b(5)(a) of the CwSV, the main contractor is jointly and severally liable with the subcontractor for the payment of contributions and advance payments on account of contributions for which the subcontractor is liable in relation to its employees. Article 16b(8) provides that the joint and several liability of the main contractor, as provided for in Article 16b(5), cannot be incurred unless the subcontractor fails to pay the contributions or advances due.

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[8] *The Minister for Labour v PMPA Insurance Co.* (1986) 5 JISLL 215

[9] Section 13 of the 1993 Act. The reason for including this provision was to prohibit a company from evading its statutory obligations through the employment of a temporary agency worker (the so-called "triangular" relationship).

[10] The purpose of CwSV was, first, to coordinate the various branches of social security (unemployment, sickness, invalidity etc.) with each other, in particular by establishing a single contribution, and, secondly, to coordinate the various branches of social security with Netherlands legislation on the taxation of wages and salaries, in particular by defining common concepts and establishing identical rules for collection.

The liability of the main contractor is subject to two qualifications:

- First, it cannot be incurred if there is any reason to believe that non-payment of the sums due is not attributable either to the main contractor or to the subcontractor (Article 16b(9) CwSW).
- Secondly, the main contractor may seek to guard against such liability by paying into a frozen account, opened in the name of the subcontractor, the part of the price payable to the latter which corresponds to the contributions. The account must be opened with a banking institution and be used exclusively for the payment of contributions.

It appears in any event that the main contractor may incur liability even if he acts in good faith. No proof of fraud is required by Dutch legislation: as a matter of fact, the principle established by the Netherlands legislation that the main contractor is to be liable is not based upon the existence of an employer-employee relationship between the main contractor and the workers in respect of whom the contributions are payable, but follows from the fact that the main contractor used the services of a subcontractor, who did not pay the social contributions for which he was liable in relation to the activities of his workers within the context of works commissioned by the main contractor. Thus, under Article 16b(5) and Article 16b(8) of the CwSV, that contractor is not, strictly speaking, liable to pay social contributions. In fact, he has to compensate the Bedrijfsvereniging for its loss of revenue by reason of the employer's non-payment of social contributions.

Finally, this rule was extended to the clothing sector by the *Law on Ultimate Responsibility in the clothing industry*, which came into force of 1994, allowing the authorities to claim tax and social security debts of subcontractors (usually clothing workshops) from contractors.

1.6 Portugal

Portugal introduced joint and several liability of the main contractor only for the case of temporary agency workers. As will be explained below, this rule only applies when the agency is found to have violated the law, and not in case of insolvency of the agency vis-à-vis its workers. According to Portuguese law, temporary work consists in the situation where one enterprise, in return for a fee, places one or more workers temporarily at the disposal of another user enterprise. (*locação de trabalhadores* or *empreitada de mão-de-obra, i.e.* hiring-out of labour.) This form of employment was regulated in Portugal in terms similar to those of French law[11].

Technically, this relationship is established through the conclusion of a tripartite relationship composed by two separate contracts:

- a contract for services between the lessor enterprise (temporary-employment agency) and the user, in which the former undertakes, in return for a fee, to place workers at the disposal of the latter;
- and a contract of employment concluded between the lessor and the temporary worker being hired out, the special nature of which lies in the fact that the worker undertakes to perform work in user enterprises[12].

Posted workers are entitled to the minimum rate of pay set in the law and to annual leave, holiday and end-of-year allowances proportional to the duration of their placement contracts[13]. Although this form of employment is not prohibited, Portuguese law has adopted a restrictive position in regard to it.

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[11] Decree-Law No. 358 of October 17, 1989.
[12] Codigo do Trabalho, Article 322.
[13] Article 21 of Decree-Law No. 358/89, of 17 October, as amended by Law No. 146/99, of 1 September.

First, the setting-up and operation of temporary-employment agencies are regulated in fairly stringent terms, having been made conditional on a series of formalities such as the need to obtain a licence and to deposit a sum of money as a guarantee. Second, the situations in which contracts to use such temporary work may be concluded are delimited: to replace existing employees who are absent or prevented from working; to fill jobs which are temporarily vacant; to cope with a temporary or exceptional increase in workload; and for short-lived or seasonal tasks. Maximum limits of from six to twelve months are imposed on the use of such workers[14].

This form of work involves a kind of "division" or "sharing" of the employer's powers: the legal employment relationship is established and always maintained with the employing enterprise (temporary-employment agency), but during the performance of work it is the user enterprise which exercises the employer's managerial authority over the worker. Disciplinary power and responsibility for paying the worker rests on the temporary-employment agency (which is deemed in law to be the sole employer), and the law stipulates that the temporary worker should receive the same pay as the user enterprise's other employees. The user enterprise becomes jointly and severally liable for this pay only in cases where its use of temporary workers is found to have contravened the law. For all other cases in which the temporary-employment agency fails to fulfil its obligations, the temporary worker may apply to be paid by the administrative authorities out of the guarantee sum previously deposited with them by the agency.

1.7 Spain

In Spain a number of provisions were introduced in the past few years, which can be considered as providing for joint and several liability of the main contractor. Already in 1995, article 42(2) of the Ley del Estatuto de los Trabajadores established joint and several liability of the principal contractor regarding wages and (under certain conditions) social security obligations[15]. According to this provision, main contractors have to demonstrate that their contractors or subcontractors are legally fulfilling their social security obligations, and for this reason must consult the General Treasury of Social Security (*Tesorería General de la Seguridad Social*), which should issue such certification within 30 days. If the Treasury has not issued any certificate within the specified deadline, the main contractor will be considered as exempted from responsibility. Apart from this case, in all other instances the main contractor will be held jointly liable for payment of wages and social security obligations for all the validity of the contract[16].

The rule differs in the case of temporary work. Under Article 16.3 of Spanish Act 14/1994, the user enterprise, which receives the services of temporary workers, in principle has only a secondary liability for wages and social security obligations owed by the temporary work agency. However, when the transfer of manpower is reputed unlawful the user enterprise is jointly and severally liable. This provision was later amended by the *Ley sobre el desplazamiento de trabajadores en el marco de una prestación de servicios transnacional* – which transposed the Posted Workers Directive in Spain[17].

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[14] Articles 18 and 19 of Decree-Law No. 358/89, of 17 October, as amended by Law No. 146/99, of 1 September.

[15] Real Decreto Legislativo 1/1995 of 24 March.

[16] In principle, under Spanish labour law the user enterprise is not responsible for the contractor's duties regarding awards, back pay or reinstatement due to dismissal of its employees. Exceptionally, the user enterprise will be responsible, when the agreement between the contractor and user enterprise has been made with the intention of defrauding workers' rights. In this case, according to Article 43.2 Employees' Statute the employees have the right to indefinite reinstatement by either the contractor enterprise or the user.

[17] Law 45/1999 of November 29.

According to this law, there are a number of minimum terms of employment that employers in the EEA[18] must guarantee to their employees relocated temporarily to Spain[19]. Failure to meet the minimum working conditions in considered to be administrative infringement. The Spanish customers or recipients of the service performed by posted workers will thus be held liable towards these workers of all the obligations and the responsibilities foreseen by Spanish legislation, independently of the nationality of the temporary work agency or of the subcontractor.

On 2 March 2001, the government introduced a decree to reform the labour market[20]. In cases of subcontracting, the decree provides that the main employer is jointly responsible for the wage and social security obligations of the subcontracting companies, and is obliged to check that the subcontractor is complying with social security payments before initiating the relationship. Later, the Ley General Tributaria 58/2003 of 17 December imposed on the principal contractor a deficiency guarantor's liability regarding the social security contributions[21].

1.8 UK

As in the case of Ireland, also in the UK client liability rules have not been enshrined in legal statutes. The United Kingdom has not introduced any specific rule concerning the provisions of domestic law applicable to posted workers but has simply expanded, where necessary, the scope of its domestic law. Employment rights and protections are directly linked to a worker's employment status – i.e., they depend largely on whether or not the worker is classified as an employee. Only employees are entitled to the full range of employment rights, including protection from unfair dismissal. On the other hand, atypical workers – including most workers on a temporary agency work contract – are treated differently from, and usually at a disadvantage compared to, employees.

Client liability for fulfilment of contractual obligations towards temporary agency workers has been subject to a hectic debate in the past few years. In most EU Member States the agency worker is, in law, an employee of the temporary work agency and enjoys the same or similar protections and rights as any other employee. To the contrary, there is no requirement under UK law for agency workers to be employed either by the agency or by the client company. Most agency workers in the UK are not employed by the agency or by the client company. An example in which temporary agency workers have been found to hold an "implied contract" with the user enterprise include the landmark appeals decision in *Dacas v. Brook Street Bureau* (2004), described in Appendix C.

As regards the construction sector, under the **UK** *Inland Revenue Construction Industry scheme* introduced in 1999, building industry contractors may only pay their subcontractors gross if they hold a particular certificate from the Inland Revenue. This measure is one of the most recent in a long line of initiatives that have attempted to regulate casual labour in the construction industry.

[18] The EU plus Norway, Switzerland, Iceland and Liechtenstein.

[19] These include working time, pay (which must be at least that provided for the same post under the relevant legal provision, regulation or collective labor agreement), equality of treatment, the rules on underage work, prevention of occupational risks, nondiscrimination against temporary and part-time workers, respect for privacy, for dignity, rights of strike and assembly, and the freedom to join a labor union.

[20] Ley 12/2001, 9 July 2001.

[21] Ley General Tributaria 58/2003 of 17 December, Article 43(1)(f).

2 New Member States

The majority of the CEE new Member States and candidate countries have launched targeted policies to combat undeclared work over the past few years[22]. Below, we focus on two main issues: existing policies on temporary agency work, and existing rules in newly enacted or reformed Labour Codes, which address similar problems to those tackled by client liability rules.

The most relevant examples of recent legislation on temporary agency work (TAW) include the new law passed in October 2004 in the Czech Republic, which defined temporary agency work and assured equal treatment on pay for temporary agency workers and permanent workers in the client company. The employment agency and the client company must ensure that the agency worker's pay and working conditions are comparable with those of the client company's employees doing the same or similar work. The agency remains responsible for paying the worker even if the user company fails to pay the agreed fee in due time. Other countries that have passed legislation to ensure equal treatment to temporary agency workers and permanent employees are Latvia, Poland, Slovakia, Slovenia, Lithuania and Hungary[23].

In many CEE countries, Labour codes have been amended or thoroughly reformed over the past few years. Countries such as the Czech Republic, Estonia and Romania have chosen to reinforce record-keeping obligations and the powers and functions of labour inspectorates[24]. Against this backdrop, only in a limited range of cases client liability rules or similar rules have been introduced. For example, Hungary is considering the introduction of a client liability rule in an amendment to the current Labour Code. The draft law stipulates that if an agency fails to meet the legal criteria or there is no appropriate employment contract, it is assumed that an employment relationship with the user enterprise exists from the date in which the agency worker started working, and for the period specified in the contract between the agency and the user. This rule is imported from the German and Austrian legal systems with the aim to make the user enterprise responsible for the lawful employment of agency workers. It will arguably be backed by fines imposed by labour inspectors.

In early 2006, Lithuania's National Labour Inspection (VDI) recommended amending a number of items of legislation, including the Criminal Code, the Code of Administrative Violations of Law and some government decrees. These amendments are intended to tighten employers' responsibility for non-fulfilment of legitimate requirements by their agents, and to supplement the list of documents that can be deemed as documentary proof of illegal work. Moreover, VDI proposes that users of illegal work should be deprived of licences to engage in particular activities for a certain period of time.

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[22] In order to evaluate the situation in the ten new Member States which joined the European Union on 1 May 2004, the Commission has commissioned a series of studies by independent experts which will look at the implementation of all directives relating to labour law. These studies are expected to be finalized in the first half of 2007.

[23] In Latvia agency work is governed by the same rules which apply to fixed-term contracts. According to the 2003 Polish Temporary Agency Work Act, the agency must notify the user company in writing of the principles and conditions governing remuneration of the temporary agency workers. Legislation regulating TAW was introduced in 2002 in Slovenia and in February 2004 in Slovakia. The Lithuanian Labour Code stipulates that a person shall exercise the right to work either by concluding an employment contract directly with an employer, or through the mediation of an employment agency. In Hungary, Act XVI of 2001 amended the Labour Code to harmonise it with many EU Directives, and included a new title on temporary agency work (*munkaerőkölcsönzés* – "employee leasing"). The 2001 legislation is based on the so-called "triangle" principle, i.e. the temporary work agency signs a contract with the employee on the basis a special sort of employment relationship, while there is a commercial contract between the agency and the user enterprise on the assignment. Source: EIRO.

[24] In Estonia, the Employment Service Act entered into force in June 2000 lists different types of employment services, which include "employment mediation". In their activities, enterprises dealing with TAW are directed mainly from the 1992 Employment Contracts Act and 2002 Law of Obligations Act. If the companies' activities are directed to other EU member states, then they have to comply with Directive 96/71/EC.

In Slovakia the new act concerning undeclared work was approved in February 2005 and came into force on 1 April 2005[25]. Employment is considered illegal when the employed person is a foreigner without permission for a temporary stay in Slovakia for the purpose of employment. The new act also considers job mediation that does not comply with the act on employment services as illegal employment performance. The undeclared work covers Slovakian citizens as well as foreigners working in Slovakia.

The Slovenian government adopted a "programme for discovering and preventing undeclared work and employment" already in 1997. A governmental commission was established to determine, coordinate and monitor activities and measures in this area[26]. The major legislation concerning undeclared work is the 2000 Law on the Prevention of Black Work and Employment (LPBWE), which defines what it refers to as "black" work and employment, the participants involved in such work and illicit advertising. Undeclared employment is defined in Article 5 of the LPBWE as occurring when a legal entity or a private person, itself fulfilling the conditions for carrying out an activity, employs a foreigner or a person without Slovene citizenship contrary to the regulations on the employment of foreigners; or when an individual, on his or her own account, employs a worker who then performs undeclared work.

3 Concluding remarks

Table 1 below summarises the main differences between national experiences in introducing client liability for the provision of cross-border services. Two of the surveyed countries, UK and Ireland, do not expressly apply joint and several liability, also in light of their common law tradition and their highly deregulated labour market. To the contrary, all other surveyed countries apply systems of joint and several liability, which however differ among themselves. In some cases (Germany, Spain and the Netherlands) national law allows workers to claim directly and immediately against the main contractor; in others (Austria), the general contractor cannot be held liable until redress has first been sought against the actual employer. In addition, some countries apply chain liability only in specific sectors (the Netherlands), whereas others only introduced rules for temporary work (Portugal). Moreover, the nature and purpose of the liability differs, as in some countries – e.g., Austria – liability exists towards social security and tax authorities, whereas in other countries client liability aims at securing the protection of workers' rights. Finally, the legal consequences of client liability differ amongst surveyed countries: on the one hand, in Germany, Austria and the Netherlands liability includes the imposition of fines. Conversely, in France no financial penalty is imposed on main contractors, which only have an obligation of vigilance over subcontractors.

As reported by the European Commission, advantages for posted workers credited to a regime of client liability include: a) an additional channel of redress when the employer "disappears" or becomes insolvent; b) incentive for companies which subcontract work to make sure that the situation of posted workers is "in order"; and c) dissuasion of companies from subcontracting work to companies when they doubt about their compliance with national rules. On the other hand, such a rule may also lead to a general reluctance to sub-contract foreign companies. The European Commission reportedly inquired Member States about the advisability of introducing a European framework governing client liability: opinions seem to diverge among Member States as to the proportionality of such a measure as well as on the issues of subsidiarity and coherence of civil law. According to some stakeholders, the introduction of such a rule would be at once difficult and undesirable, as existing national rules differ widely, and the notion of "client liability" is totally absent in many legal systems.

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[25] Act No. 82/2005 Coll. on illegal work and illegal employment and amendments in other related acts

[26] The commission is headed by the Secretary of State responsible for this area at the Ministry for Labour, Family and Social Affairs (*Ministrstvo za delo, družino in socialne zadeve*, MDDSZ).

Moreover, doubts arise over the consistency of such measure with principles of subsidiarity and proportionality[27].

TABLE 1 – SUMMARY OF MAIN FINDINGS

Country	Type of rule	Object	Purpose	Restrictions	Sectors	Performance Guarantee
Austria	Client liability	Wage, social sec.& tax	Protection of workers	Redress must first be sought against actual employer	All	by main contractor (only in the construction sector)
France	Financial solidarity, *culpa in vigilando*	Wage, social sec.& tax	Protection of workers	Customer liable only is performance guarantee is insufficient, and if negligent in monitoring subcontractor	All	by subcontractor
Germany	Client liability (*strict liability*)	Wage, social sec.& tax (first subcontr.); Only net pay (next subcontr.)	Protection of workers	No (*direct claim*)	All	No
Ireland	Liability of employer	Employment contract	Protection of agency workers	Only when agency workers are classified as employees (e.g. under the Unfair Dismissal Act)	All	No
Netherlands	Chain liability	Social security & tax	Payment of social security and tax	Direct claim, but: liability cannot be incurred if there is any reason to believe that non-payment of the sums due is not attributable either to the main contractor or to the subcontractor	Construction (1982) Clothing (1994)	by main contractor (frozen account)
Portugal	Joint and several liability	Wage	Protection of temporary workers	Only temporary agency workers (very limited cases)	All	by temporary employment agency
Spain	Joint and several liability (1999) + Secondary liability (2001, 2003)	Wage, work conditions + Social security and Tax	Protection of temporary workers + Payment of social security and tax	No (*direct claim*) + Redress must first be sought against actual employer	All	No
UK	Liability of employer	Employment contract	Protection of agency workers	Only when agency workers are classified as employees (e.g. *Dacas v. Brook Street Bureau*)	All	No

[27] See, e.g., UNICE.

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Appendix A: the *Wolff & Müller* case

The European Court of Justice (ECJ) recently delivered a judgment on the German rules regarding the general contractor's joint and several liability in respect of payment of the minimum wage by his subcontractors. It was also the first case decided under the Posted Workers Directive. In its Judgment of 12 October 2004 in the case *Wolff & Müller*, the ECJ found that, pursuant to Directive 96/71/EC, Member States are obliged to ensure that undertakings guarantee to workers posted in their territory the payment of minimum rates of pay[28]. In doing this, it analysed the German client liability rule introduced by the AEntG (see Section 1.3. above).

Mr Pereira Félix was a Portuguese national who, from 21 February to 15 May 2000, was employed in Berlin as a bricklayer on a building site by a construction undertaking established in Portugal. The latter carried out concreting and reinforced concrete work on that building site for Wolff & Müller. By an application lodged on 4 September 2000 with the Berlin Labour Court, Mr Pereira Félix sought payment jointly and severally from his employer and from Wolff & Müller of unpaid remuneration amounting to DM 4,019.23. He claimed that Wolff & Müller, as guarantor, was liable, under Paragraph 1(a) of the AEntG, for unpaid wages. Wolff & Müller opposed the claims by Mr Pereira Félix, arguing in particular that it was not liable as Paragraph 1(a) of the AEntG constituted an unlawful infringement of the constitutional right to carry on an occupation under Article 12 of the Grundgesetz (Basic Law) and also of the freedom to provide services enshrined by the EC Treaty. The Berlin Labour Court upheld the claim by Mr Pereira Félix. The Higher Labour Court, before which the case was brought by Wolff & Müller, partially dismissed its appeal, whereupon it appealed on a point of law to the Federal Labour Court.

In its judgment, the ECJ pointed out that the protection of workers is one of the overriding reasons relating to the public interest capable of justifying restrictions on the freedom to provide services. The ECJ then concluded that the freedom to provide services does not preclude joint and several liability to protect minimum remuneration, even if the safeguarding of workers' pay is not the primary objective of the legislation or is merely a subsidiary objective[29].

In *Wolff & Müller*, the ECJ held that Article 5 of the Posted Workers Directive, interpreted in the light of Article 49 EC, does not preclude the use of a system of joint and several liability as *"an appropriate measure in the event of failure to comply with [...] Directive [96/71/EC]."* Furthermore, it held that such a measure encourages compliance with the Directive and may, in this sense, count among the instruments destined to ensure effective and widespread implementation of the Directive provided it is proportionate to the objective pursued. As noted by Hellsten (2006), since the ECJ in *Wolff & Müller* found a wage liability scheme with joint and several responsibility to be compatible with the free provision of services, the corresponding wage liability schemes analysed above in this briefing note are likewise to be regarded as restrictions that are compatible with EC law: "[t]he opposite would normally require a striking discriminatory element to be inherent in a given national scheme"[30].

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[28] Case C-60/03, *Wolff & Müller GmbH & Co. KG v José Filipe Pereira Félix.*
[29] The Court left it to the referring court to carry out the assessment of whether this measure is proportionate.
[30] Hellsten (2006), at 51.

Appendix B: the UK *Dacas* case

A recent case decided by the UK Court of Appeal can shed some light on the protection of temporary agency workers in the UK. Although the approach adopted by the Court is not consolidated in the UK and elicited a fierce debate, it seems useful to briefly describe the rationale adopted by the Court to devise an implied contract between an agency worker and its user undertaking.

In *Dacas v. Brook Street Bureau*, the main issue was whether a temporary worker (Mrs Dacas) engaged by an agency to work for a user enterprise (*Wandsworth Council*) was actually an employee of that user[31]. The initial decision of the Employment Tribunal had been that Mrs Dacas had no employer at all. However, the Employment Appeal Tribunal (EAT) found that Mrs Dacas was an employee of the employment agency (*Brook Street*) which had placed her with the Council.

The Court of Appeal overturned the EAT's decision and found that Wandsworth Council (the user) was in fact her employer, and that Brook Street was not. Interestingly, Mrs Dacas had no contract of employment with Wandsworth Council for whom she worked, and it was the employment agency which was contractually bound to pay her salary. In the Court's view, the contractual document between Mrs Dacas and the employment agency was important, but it was not necessarily determinative of the contractual employment relationship. The Court described this type of arrangement as a "triangular arrangement": Mrs Dacas did work for the user at the user's premises under the control of the user; the user indirectly paid Mrs Dacas for the work done by means of regular payments to the employment agency calculated according to time sheets submitted by the Applicant.

As a result, the Court plainly stated that the parties should nonetheless be prepared to accept that an employment relationship existed between Mrs Dacas and either the end-user or the employment agency. The question of which party really exercised day to day control over the temp and her work activities was crucial to determining which party was her employer. The Council probably did not intend to enter into a direct contractual relationship with Mrs Dacas, but it did exercise day-to-day control over her activities and over her in the workplace; the agency did not, it only supplied the temp as required. Between the Council and Mrs Dacas there was an implied contract of service: therefore, Mrs Dacas was an employee of the Council[32].

In light of this decision, employers who regularly use temporary agency workers and keep these workers on their books for many months or even years, should be aware that an implied contract of employment may exist between them and the temp worker. This would bring with it unfair dismissal rights, vicarious liability and other usual obligations between employer and employee.

[31] Dacas sued Brook Street Brueau for unfair dismissal. See [2004] EWCA Civ 217.

[32] One of the judges (Sedley LJ) expressed the view that, after completion of a year's service (at which time the employee would accrue unfair dismissal rights), it should be sufficiently clear whether an implied contract of employment has arisen. He also appeared to suggest that this would usually be a contract with the end-user. However, it is not altogether clear at what point in time this agreement may be implied, and indeed many statutory employment rights are not conditional upon the employee having 12 months' service.