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Intra-group loans of employees can be considered As an illegal supply of employees or as an illegal subcontracting of labor

In a decision dated May 18, 2011 (Cass.soc., n° 09-69.175), the Labor Chamber of the *Cour de Cassation* (French Supreme Court) further clarified the notion of illegal supply of employees within the context of a loan of employees from a parent company to one of its subsidiaries.

1. The loan of employees may result in companies being liable for two different offenses: the illegal supply of employees (*prêt illicite de main d'œuvre*) and the illegal subcontracting of labor (*marchandage*)

Illegal supply of employees

Article L.8241-1 of the French Labor Code stipulates that "*any profit-making operations, the sole purpose of which is the supply of employees, is forbidden*".

This provision does not apply to temporary working agencies, *portage salarial****[1]***, job-sharing employment agencies, model agencies and sports associations.

Conversely, "*loans of employees for non-profit purposes are authorized*" (Article L.8241-2 of the French Labor Code).

Failing to comply with these provisions exposes employers to a fine of EUR 30,000 and two years' imprisonment. The Court may also prohibit the relevant company from subcontracting employees for a period of 2 to 10 years (Article L.8243-1 of the French Labor Code).

For legal entities, the maximum fine is five times the amount set forth above, in accordance with Article 131-38 of the French Criminal Code.

Illegal subcontracting of labor:

Article L.8231-1 of the French Labor Code defines illegal subcontracting of labor as "*the supply of labor on a profit-making basis when it has the effect of causing loss or harm to the employee or evading legal rules or applicable provisions of collective agreements*".

The illegal subcontracting of labor is of course prohibited.

The loan of employees must be distinguished from a services agreement for profit purposes that is perfectly legal. In such a case, a particular attention must be paid to the link of subordination: in no event must the employees of the lending company be placed under the authority of the user company. The latter must not act as an employer and exercise the subordination link that is a distinctive feature of an employer-employee relationship.

The offenses of illegal supply of employees and illegal subcontracting of labor are characterized by the existence of the notion of profit-making. This notion may lead to various interpretations and several decisions of the *Cour de Cassation* have clarified its boundaries.

In its decision dated May 18, 2011, the Labor Chamber of the *Cour de Cassation* provided further insight into this notion.

2. The decision of May 18, 2011: a parent company and its subsidiary fined for illegal supply of employees and illegal subcontracting of labor

In this case, employees had been hired by the parent company to be subsequently loaned to a subsidiary. Salaries were paid by the parent company that re-invoiced to its subsidiary the salary costs and related social contributions. The collective bargaining agreement in force within the parent company applied to the employees.

In its decision, the Labor Chamber of the *Cour de Cassation* recalled that the prohibition to loan employees for profit-making purposes set forth in Article L.8241-1 of the French Labor Code applies both to the lending company and the user company. None of them must derive a financial gain or advantage from the loan of employees.

The Labor Chamber of the *Cour de Cassation* specified that "***the profit-making nature of the loan may result from increased flexibility in staff management/administration and savings in social charges enjoyed by***" the user company. Having recalled this principle, the Labor Chamber noted that the subsidiary had not incurred any staff management expenses, apart from the reimbursement of the salaries and social charges on a Euro for Euro basis. The Labor Chamber held that the situation was, therefore, constitutive of an illegal loan of employees.

The attention of companies should be drawn to the definition of the "profit-making" given by the Labor Chamber of the *Cour de Cassation* and to the two criteria used in this respect.

It should first be noted that the two criteria seem to be cumulative. In addition, it seems that the terms "savings in social charges" has been used by the *Cour de Cassation* in very broad sense. We believe that limiting its interpretation to management/administration costs only would be dangerous in the future, even if in the case at hand such costs were not re-invoiced. Re-invoicing management costs is, therefore, essential but insufficient.

As such, insofar as the profit-making nature of a loan of employees is established when the user company benefits from savings in social charges, any company using employees under such a loan must make sure that it does not derive any gain or benefit from this situation (such as for example savings in relation to the financing of a works council, the costs of social protection, etc.).

At the same time, it is necessary to ensure that the lending company also does not derive any gain or benefit from the loan of employees. In practice, complying with these two requirements will be difficult when the two companies have a different size, operate in a different industry (e.g. a holding company and a subsidiary operating in the manufacturing industry) and are, consequently, subject to quite different social obligations and social charges.

In addition, the first criteria set out by the Labor Chamber of the *Cour de Cassation* raises a concern. Can the increased flexibility in staff management/administration alone be used to establish the profit-making nature of a loan of employees? Time will tell.

What will be the position of the courts when a company will have to dismiss on economic grounds employees whose loan is interrupted by the user company? The user company will necessarily make savings as it will not be responsible for termination costs. How can the lending company assign such termination costs to the user company? Legally speaking, the lending company remains the sole employer and, as such, the interruption of the loan cannot in itself serve a ground for termination.

Disputes can easily arise in this respect. Loaned employees who may not benefit from the provisions of a lay-off plan because they administratively report to the lending company whereas they have carried out their employment duties within the user company during the whole duration of their employment contract could easily obtain from the court the recognition of the existence of an illegal subcontracting of labor.

It should be specified here that the notion of co-employer is increasingly used in labor disputes concerning companies of the same group.

As such, concerning the offense of illegal supply of employees, we can consider that significant risks exist for companies that wish to loan employees on a long-term basis and that use such loans as a mode of management/administration of employees especially hired to be subsequently loaned to another entity, even if that entity belongs to the same group.

This type of long-term loan, for the benefit of a single entity, is also likely to constitute a second offense – like in the commented decision: the illegal subcontracting of labor.

As explained above, the offense of illegal subcontracting of labor is established when such subcontracting has the **effect** of causing loss or harm to the employee or evading legal rules and or applicable provisions of collective agreements.

The complexity and diversity of labor provisions – including in respect of social protection – applicable to employees and employers make it very easy to establish the offense of illegal subcontracting of labor.

It merely requires raising the major discrepancies between two collective bargaining agreements, between the benefits granted to the employees of a large company and the benefits granted to the employees of a very small business, or between two companies operating in quite different industries and, therefore, subject to quite different collective bargaining agreements.

In the commented decision, a loaned employee challenged the application of the time-by-day method (*forfait jours*[2]) while the collective bargaining agreement applicable within the user company did not provide for this working time management method. He claimed that this situation was prejudicial to him. The Labor Chamber of the *Cour de Cassation* agreed with the arguments of the employee and acknowledged the illegal subcontracting of labor.

3. Practical consequences for groups of companies

Group companies are strongly recommended to loan employees exclusively when it is justified to do so by specific circumstances and for a period time corresponding to the effective assignment to be performed by the to-be-loaned employees. In addition, it is essential to re-invoice all of the costs – including notably the staff management/administration costs. As such, in the absence of any profit-making implications, the offenses of illegal supply of employees and illegal subcontracting of labor should be excluded.

For long-term assignments, it is imperative to check whether the contemplated operation will be likely to cause a harm or loss to the to-be-loaned employees. In particular, it will be necessary to compare the employees' collective status in the lending company and user company.

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[1]The French system of *portage salarial* is defined as a unity of contractual relationships organized between a portage company (umbrella company), an independent contractor and a customer company. Basically, 2 contracts are established: (i) a service contract between the umbrella company and the customer company and (ii) a temporary employment agreement between the independent contractor and the umbrella company. When the service is performed by the independent contractor, the customer company pays the fees to the umbrella company that subsequently pays to the independent contractor a salary. The *portage salarial* is sometimes summarily referred to as a halfway house between self-employment and being an employee.

[2] System of calculating working time, in days per year rather than hours per week.