The relations between German employers and employees are extensively regulated under German labour and employment law. Set out below are certain important issues, regulated by law, which must be considered when entering into an employment agreement and terminating such employment agreement:

1. Employment Agreement
The following issues must be considered when the employment agreement is drafted:

Written Form
It is common that German employees have written employment agreements, reflecting the key aspects of the employment relationship (e.g. parties to the agreement, work to be performed, gross salary and benefits, vacation, starting date of employment, place of performance and notice periods). However, such written form is not mandatory – also oral employment agreements are valid.

Working Time
All weekdays excluding Sundays and public holidays are considered by law to be working days. However, German employees usually work from Monday to Friday (five-day week).

Under a five-day week, typically, the average working time is between 35 and 40 hours. The daily productive working time generally may not exceed eight hours. A daily working time of up to 10 hours productive working time is possible if – over a period of six months – the average daily working time does not exceed eight hours.

Working on Sundays and public holidays is generally prohibited. However, the German Law on Working Hours provides for several exceptions from this rule (in some cases prior approval by governmental authorities is required).

Vacation
German labour and employment law provides for a statutory claim for 20 working days’ vacation per calendar year for employees who work a five-day week (that corresponds to four weeks of vacation in total). However, it is common for an employee to be granted between 25 and 30 vacation days per calendar year by his employer. The number of vacation days granted will depend on his seniority and the employer’s field of business.

Stock Options
In addition to base salary and variable compensation (such as sales commission and bonus payments) employees are often granted stock options as an incentive. In the case of US parent companies with subsidiaries or branch offices in Germany, such options are generally granted under the respective US stock options plan.

German law does not prohibit the use of such a US plan. However, under German law any vesting periods contained in a US plan may not be lengthened to such an extent that the employee’s right to terminate the employment agreement is frustrated. We believe that in the case of, for example, a vesting of 25% of the options after one year and then a monthly vesting of 1/36 of the remaining 75% over the following three years, or a vesting on a monthly basis over the full vesting period, would not be regarded as frustrating the employee’s rights.

The granting of options or the vesting of options is not taxable in Germany. However, if an employee actually exercises vested stock options, the difference between the market price at the time of exercising the option and the price the employee has to pay for the stocks is deemed to constitute taxable income of the employee. Accordingly, any such taxable profit of the employee is processed through the payroll at the German subsidiary or branch office with applicable income tax and social security withholdings.

Regarding German securities law, there is no requirement to register or file the stock option plan or a prospectus, which is made available to German employees, with any German authority. It is also not required that a prospectus available to German employees must be in the German language. A summary of applicable laws on insider trading should be made available to the German employees.

Fixed Term Employment Agreement
Although an employment agreement unlimited in time is typical for Germany, it is possible to agree on an employment agreement with a limited (i.e. fixed) term (and employers tend to increasingly make use of this possibility). Fixed term employment agreements are, however, subject to restrictions under German labour and employment law. Generally, a fixed term employment agreement is permissible only when there is an objective reason for the limitation (e.g. substitution in case of illness, project work).

However, an employer can always enter into a fixed term employment agreement for a period of up to two years, without restrictions (and renew it three times within said period, up to a maximum of two years). Additionally, newly founded companies can enter into fixed term employment agreements for a period of up to four years, without restrictions. Fixed term employment agreements always require written form as otherwise they are deemed to be concluded for an indefinite period of time.
Independent Contractors
German companies often engage independent contractors for the provision of certain services, as they benefit from independent contractors being neither subject to protective provisions of German labour and employment law (such as termination protection) nor being insured by the mandatory state-run social security system. Companies should, however, act with caution, since German social security courts and the authorities charged with overseeing the system, regard an individual as an employee and not as an independent contractor — no matter what the underlying agreement may say — if the individual “personally depends” on the contractual partner. In general, such personal dependence is assumed if the contractual partner has — according to the provisions of the agreement or the course of conduct of the parties — the right to give instructions to the engaged person, in particular with respect to the place, duration, content, execution and time of performance, and if the engaged person is integrated in the contractual partner’s business. If a company treats the engaged person as an independent contractor and it is later determined that the engaged person actually had an employee position, the company has to pay all contributions to social security providers (employer’s and employee’s shares) retrospectively for the full period of the employment term (but with the retrospective effect being limited to a maximum period of four years). Additionally, the engaged person benefits from termination protection and may claim to be treated according to protective provisions of German labour and employment law.

Maternity and Parental Leave
Female employees are entitled to full paid maternity leave (starting no later than six weeks before the expected due date, but depending on the mother’s and baby’s health situation and the work performed by the woman, and ending eight weeks after childbirth). Payments to the employee are made partly by the statutory health insurance provider and partly by the employer. During the employee’s pregnancy and during a period of four months after childbirth, no termination of the employment relationship by the employer is permissible.

All employees, both male and female, are entitled to a maximum of three years’ parental leave per child. During this period the employer is not obliged to make any payments to the employee. However, the employer may not terminate the employee. Employees have a legal right to work part-time (up to 30 hours per week) during parental leave. After expiry of the parental leave, the employer has to offer an adequate working position to the employee.

Works Council
In companies with more than five employees, the employees may elect a works council. The works council represents the employees and negotiates cooperates and consults with the employer in various situations (e.g. hiring of new employees, changes to the place of business, shut down of the business, mass lay-offs).

3. Termination of the employment agreement
German employment termination law is intended to protect the employee against unfair dismissal.

Termination Notice Period
The employer must observe the applicable notice period, which is ordinarily determined by law (between four weeks and seven months, depending upon the length of employment). If the employer and the employee have mutually agreed upon a longer contractual notice period, the longer contractual notice period will prevail. Any agreement on a notice period that is shorter than the applicable statutory notice period will be invalid. Generally, an employment can only be terminated with effect as of the end of any calendar month. The employer must therefore keep the effective date of employment termination in mind when calculating when to deliver the termination notice.

Written Form
The employer has to give a written notice of termination to the employee. The document has to be signed by the employer. All other forms of notice of termination — for example those given orally or by email or fax — are void and have to be redone in a proper way.
Restriction of Termination
The termination of an employment is restricted provided that (i) an employee has been employed for more than six months when the notice of termination is given and (ii) the employer employs more than 10 full-time employees. An employee, who fulfils these requirements, may further only be terminated for a “particular reason”, including but not limited to (i) reasons related to the personal situation of the person to be dismissed (e.g. long-term sick leave), (ii) reasons related to the behaviour of the person to be dismissed (for example theft or fraud to the detriment of the employer) or (iii) reasons related to the business of the employer (for example the employer’s decision to restructure the business, which reduces the number of positions).

Special Termination Protection
Special termination protection against unlawful dismissal applies to employees who are officially acknowledged handicapped persons, employees on three years’ maternity leave, or pregnant employees. In all of these cases, prior approval of various German authorities is required – but usually rather difficult to obtain.

Mass Lay-Off
In case a company intends a mass lay-off, which means that the employer intends to terminate a large percentage of its employees during a one-month period, the prior approval by the employment office is required.