1. The exclusion of small businesses from a national system of protection of workers against unfair dismissal, with the effect that they are not obliged to pay compensation in the event of socially unjustified dismissals or to bear the legal expenses incurred in proceedings concerning the dismissal of workers, does not constitute aid within the meaning of Article 92(1) of the Treaty.

   Such a measure does not entail any direct or indirect transfer of State resources to those businesses but derives solely from the legislature's intention to provide a specific legislative framework for working relationships between employers and employees in small businesses and to avoid imposing on those businesses financial constraints which might hinder their development.

2. The principle of equal treatment for men and women as regards the conditions of dismissal as it emerges from Articles 2(1) and 5(1) of Directive 76/207 does not preclude the application of a national provision which does not take into account employees whose working hours are not more than 10 hours per week or 45 hours per month when determining whether or not an undertaking must apply the system of protection against unfair dismissal, where it is not established that undertakings which are not subject to that system employ a considerably greater number of women than men. Even if that were the case, such a measure might be justified by objective reasons not related to the sex of the employees in so far as it is intended to alleviate the constraints weighing on small businesses.

REPORT FOR THE HEARING
in Case C-189/91 *

I — Facts and procedure

1. *National law*

The Kündigungsschutzgesetz (Law on protection against unfair dismissal, in the consolidated version published on 25 August 1969, BGBl. I, p. 1317, as amended by the first Arbeitsrechtsbereinigungsgesetz (Law on the revision of labour law); hereinafter referred to as 'the Law on unfair dismissal') lays down the fundamental rule that 'socially unjustified' dismissals have no legal effect.

By virtue of Paragraph 1 of the Law on unfair dismissal, dismissal is socially

* Language of the case: German.

unjustified where it is not based 'either on grounds relating to the person or behaviour of the employee or on overriding needs of the undertaking which preclude the further employment of the worker by that undertaking'. Where the dismissal of an employee is disputed, the labour courts must verify the actual reasons which led the employer to dismiss the worker.

In cases where the court considers that dismissal of the worker is socially unjustified, the employment relationship must in principle be continued (principle of 'protection of acquired rights'). Nevertheless, when the court considers that the employment relationship cannot reasonably be continued, it may declare it terminated on application by the worker or, under certain circumstances, the employer. The employer is then required to pay the worker compensation in an amount not exceeding the equivalent of a year's wages (Paragraphs 9 and 10 of the Law on unfair dismissal). [1]

By virtue of the second and third sentences of Paragraph 23(1) of the Law on unfair dismissal, [2] the system of protection against unfair dismissal described above is not applicable

'to undertakings and authorities which normally employ no more than five employees, excluding persons employed as part of their vocational training. In determining the number of persons employed for the purpose of the second sentence, account is to be taken only of those employees whose normal period of work exceeds 10 hours per week or 45 hours per month.'

In those businesses and authorities (hereinafter referred to as 'small businesses'), the employer may dismiss employees after the lawful period of notice, and the courts may not review the validity of the grounds of dismissal.

2. *The main proceedings and the preliminary questions*

Mrs Kirsammer-Hack worked as a dental assistant in Mrs Sidal's dental practice, which had a total staff of two full-time employees, two employees, including Mrs Kirsammer-Hack, who worked more than ten hours per week and four employees who worked on average fewer than ten hours per week and four employees who worked on average fewer than ten hours per week or 45 hours per month.

On 13 February 1991, Mrs Kirsammer-Hack was dismissed with effect from 31 March 1991. Mrs Kirsammer-Hack considered that the dismissal was socially unjustified within the meaning of the Law on unfair dismissal, and she therefore brought an action before the Arbeitsgericht Reutlingen seeking a ruling that the contract of employment with Mrs Sidal continued to have effect after 31 March 1991.

1 — According to the national court, in practice most disputes concerning the dismissal of workers are settled by the conclusion of a 'compensation agreement', under which the employer undertakes to pay the worker compensation of between one-half and one month's salary for each year of employment. According to the national court, employers agree to enter into such compensation agreements because they recognize a 'moral obligation' towards the worker and because they thus avoid long and costly legal proceedings.

2 — The third sentence was added by Article 3 of the Beschäftigungsförderungsgesetz (Law on the promotion of employment) of 26 April 1985 (BGBl I, p. 710 et seq.).

The defendant in the main proceedings considers that the provisions of the Law on unfair dismissal are inapplicable on the ground that fewer than five employees, within the meaning of Paragraph 23(1) of the Law on unfair dismissal, work in her undertaking.

The national court shares the view of the defendant. It considers, however, that Paragraph 23(1) of the Law on unfair dismissal might be contrary to Community law.

The national court observes that small undertakings account for 10% of all German undertakings, employ approximately 10% of all employees in the Federal Republic of Germany [3] and are active in particular in the craft, agricultural, commercial and cleaning sectors. The court also points out that large undertakings could also fall outside the scope of the system of protection against unfair dismissal by employing a large number of workers whose hours of work are below the threshold provided for in the third sentence of Paragraph 23(1) of the Law on unfair dismissal (hereinafter referred to as 'part-time workers').

The national court points out that, having regard to the second sentence of Paragraph 23(1) of the Law on unfair dismissal, small businesses cannot be required to compensate workers whose dismissal is socially unjustified. In view of the amount of the compensation paid in cases of socially unjustified dismissal and to the legal expenses incurred in proceedings concerning the dismissal of workers, small undertakings have a great competitive advantage in relation to other undertakings. Indeed, that situation is one of the objectives pursued by the German legislature.

Referring to the order of the Arbeitsgericht Bremen of 9 October 1990 in the *Sloman Neptun* cases (Joined Cases C-72/91 and C-73/91, still pending), the national court considers that the second sentence of Paragraph 23(1) of the Law on unfair dismissal could constitute an aid to small businesses which is incompatible with the common market and thus contrary to Article 92(1) of the EEC Treaty.

However, even supposing that Paragraph 23(1) of the Law on unfair dismissal does not constitute an aid within the meaning of Article 92(1) of the Treaty, that provision might, according to the national court, be incompatible with Community law for another reason. The third sentence of Paragraph 23(1) of the Law on unfair dismissal constitutes, in its view, indirect discrimination against women.

The national court notes that by virtue of Article 5(1) of Council Directive 76/207/EEC of 9 February 1976 on the implementation of the principle of equal treatment for men and women as regards access to employment, vocational training and promotion, and working conditions (OJ 1976 L 39, p. 40), 'application of the principle of equal treatment with regard to working conditions, including the conditions

3 — According to the national court, the figures should increase in the future. Three factors explain that growth, namely: (1) increasing scope for the use of capital rather than labour; (2) the advantages for the employer of employing workers part time (savings on social insurance); and (3) the advantages for the worker of part-time work (lower tax rate).

governing dismissal, means that men and women shall be guaranteed the same conditions without discrimination on grounds of sex'. Furthermore, Article 2(1) of Directive 76/207 states that, within the scope of that directive, prohibition of discrimination based on sex covers not only direct discrimination but also indirect discrimination.

Moreover, the national court points out that the great majority (90%) of workers whose hours of work fall below the threshold laid down in the third sentence of Paragraph 23(1) of the Law on unfair dismissal are women. Consequently, most of the undertakings which are excluded from the scope of the system of protection against unfair dismissal because of the number of part-time workers they employ are undertakings which employ women on a part-time basis. The national court concludes that the third sentence of Article 23(1) of the Law on unfair dismissal constitutes indirect discrimination against women contrary to the combined provisions of Articles 2 and 5 of Directive 76/207, on which the plaintiff in the main proceedings is entitled to rely.

By order of 3 May 1991, the Arbeitsgericht Reutlingen decided to stay the proceedings and refer the following questions to the Court for a preliminary ruling:

'1. Is the exclusion of small businesses from the system of protection against unfair dismissal under the second sentence of Paragraph 23(1) of the Kündigungsschutzgesetz (Law on unfair dismissal, as amended by the first Arbeitsrechtsbereinigungsgesetz (Law on the revision of labour law) of 25 August 1969, BGBl. I, p. 1317) compatible with Article 92(1) of the EEC Treaty?

If not,

2. Does the third sentence of Paragraph 23(1) of the Law on unfair dismissal (as amended by Article 3 of the Beschäftigungsförderungsgesetz (Law on the promotion of employment] of 26 April 1985, BGBl. I, p. 710 et seq.) constitute indirect discrimination against women, contrary to Articles 5 and 2 of Council Directive 76/207/EEC of 9 February 1976 on the implementation of the principle of equal treatment for men and women as regards access to employment, vocational training and promotion, and working conditions?'

3. *Procedure before the Court*

The order of the Arbeitsgericht Reutlingen was received at the Court Registry on 25 July 1991.

Pursuant to Article 20 of the Protocol on the Statute of the Court of Justice of the EEC, written observations were submitted by the German Government, represented by Ernst Röder, Ministerialrat in the Ministry of Economic Affairs, and Joachim Karl, Regierungsdirektor in the Ministry of Economic Affairs, acting as Agents, and by the

Commission of the European Communities, represented by Michel Nolin, a member of its Legal Department, assisted by Claus-Michael Happe, a German civil servant on secondment to the Commission as part of the programme of exchanges with national civil servants, acting as Agents.

Upon hearing the report of the Judge-Rapporteur and the views of the Advocate General, the Court decided to open the oral procedure without any preparatory inquiry.

II — Written observations submitted to the Court

The first question

As a preliminary point, the *German Government* describes the aim of the second sentence of Paragraph 23(1) of the Law on unfair dismissal. It points out first of all that in small businesses relations between employer and workers are above all personal relations. The exclusion of those businesses from the system of protection against unfair dismissal reflects the wish, in the event of conflict between an employer and a worker, to avoid a situation where that relationship must be continued during any proceedings before a court and possibly afterwards. The German Government goes on to observe that it would be difficult for an employer managing a small business to bear the financial and administrative burdens arising from a dispute concerning the alleged unfair dismissal of a worker. Accordingly, small businesses are in a different situation from that of other undertakings and the system of protection against unfair dismissal applicable to those other undertakings cannot be applied to them.

On the question whether a provision such as the second sentence of Paragraph 23(1) of the Law on unfair dismissal constitutes aid which is incompatible with the common market, the German Government observes first of all that in any event only the Commission has the power to find an aid incompatible with the common market, subject to review by the Court. Consequently, so long as the Commission's examination has not been concluded individuals may not rely on the incompatibility of aid with the common market before national courts (see the judgment in Case 78/76 *Steinike & Weinlig* v *Germany* [1977] ECR 595, paragraphs 9 and 10).

The German Government goes on to draw attention to the fact that the concept of aid within the meaning of Article 92(1) of the Treaty covers not only positive benefits but also exemption from charges which businesses would normally be bound to bear. In this respect, it acknowledges that the exclusion of small businesses from the ambit of a system of protection against unfair dismissal represents, for small businesses, a double saving: first of all, they are not obliged to bear the costs of legal proceedings brought by a worker alleging that his or her dismissal was not socially justified; secondly, they are not bound to pay compensation to a worker whose dismissal is not socially justified. That cost saving for small businesses does not

mean, according to the German Government, that their exclusion from the ambit of the protection against unfair dismissal constitutes an aid.

With regard to the saving by small businesses on the expenses of legal proceedings — and the loss, by the State, of court fees in relation to those proceedings — the German Government states that that saving is not the direct result of the non-application of the system of protection against unfair dismissal. Where the system is applicable, the bringing of an action for a declaration that the dismissal was not socially justified is left to the initiative of the worker concerned. Moreover, although the system of protection against unfair dismissal is not applicable to small businesses, various rules, such as those concerning notice of dismissal and dismissal in the context of the transfer of a business, do apply to small undertakings. Therefore, small undertakings might well have to bear the cost of proceedings concerning the dismissal of a worker.

With regard to the saving on the compensation paid to a worker whose dismissal is not socially justified, the German Government states that the payment of such compensation is not the direct result of the application of the system of protection against unfair dismissal: first of all, the purpose of that system is to ensure the continuation of the employment relationship, not the payment of compensation to the worker, where the dismissal is not socially justified; secondly, where the dismissal is not socially justified, the employer can only be required to pay compensation where the employment relationship cannot be maintained and the contract is terminated on request of one of the parties. Moreover, it is not out of the question that, even in a small business, the employer may offer compensation to a dismissed worker. Finally, in the context of the system of protection against unfair dismissal any compensation which may be due to the worker is paid by the employer and is not financed by public funds. The German Government points out that, were the system of protection against unfair dismissal to be extended to small undertakings, in view of the size of the financial burden represented by compensation, it would have to be financed by a system of contributions from all the undertakings involved. It observes in this respect that such a system would penalise undertakings which rarely dismiss workers.

Moreover, the German Government notes that the second sentence of Paragraph 23(1) of the Law on unfair dismissal, far from exempting small undertakings from public charges, constitutes legislation on working relations between employers and workers. That legislation is the expression of a general economic policy aimed at promoting small and medium-sized undertakings. That policy is consistent with one of the objectives of the Community, expressed in Article 118a of the Treaty, and implemented by Council Decision 89/490/EEC of 28 July 1989 on the improvement of the business environment and the promotion of the development of enterprises, and in particular small and medium-sized enterprises, in the Community (OJ 1989 L 239, p. 33).

Finally, the German Government considers that the second sentence of Paragraph 23(1) of the Law on unfair dismissal is not contrary to the first paragraph of Article 117 of

the Treaty. That provision, which states that 'Member States agree upon the need to promote improved working conditions and an improved standard of living for workers, so as to make possible their harmonization while the improvement is being maintained', is in the nature of a programme and does not impose concrete obligations on the Member States (see the judgment in Case 149/77 *Defrenne* v *Sabena* [1978] ECR 1365, paragraphs 19 to 23 and 30 to 32).

In view of the foregoing, the German Government proposes that the Court inform the national court that the second sentence of Paragraph 23(1) of the Law on unfair dismissal does not constitute aid prohibited by Article 92 of the Treaty.

The *Commission* points out that since small undertakings are excluded from the ambit of the general system of protection against unfair dismissal they are practically never willing to pay compensation to a dismissed worker. Even though the Law on unfair dismissal envisages payment of compensation only in exceptional cases, the Commission considers that that compensation constitutes a cost normally borne by undertakings and that it must be regarded as a state measure because its payment is the direct consequence of the system introduced by the Law on unfair dismissal, which is of general application.

However, referring to the judgment in Case 173/73 (*Italy* v *Commission* [1974] ECR 709, point 15), the Commission considers that the exemption of small undertakings from the ambit of the system of protection against unfair dismissal constitutes an aid covered by Article 92 of the Treaty only if that exemption is not justified on the basis of the nature of the system of protection which has been introduced.

It points out in that respect that the system established by the Law on unfair dismissal is based on the principle of 'protection of acquired rights', by virtue of which dismissal of an employee by his employer does not affect the continuation of the employment relationship unless the dismissal is socially justified.

In smaller firms 'there is a closer relation of trust between employer and employees based on personal knowledge and, secondly, because it is believed that disputes arising in such production units are difficult to settle' (Labour Law and Industrial Relations in Small and Medium-sized Enterprises in the EEC Countries — Commission Investigation Report, Luxembourg 1988, p.45). Consequently, it would be difficult for the employment relationship between an employer running a small undertaking and an employee whom he has dismissed to be continued where that dismissal does not appear to be socially justified. In a small undertaking the employer would frequently be obliged to pay compensation to an employee whose dismissal is not socially justified. Accordingly, to apply the Law on unfair dismissal uniformly to undertakings regardless of their size would place small undertakings at a considerable disadvantage. In that respect, the fact that disputes concerning the issue whether or not a dismissal is socially justified are generally settled out of court by way of a compensation agreement is irrelevant because such settlement is not provided for in the Law on unfair dismissal and may not therefore be taken into account in examining the system introduced by those rules.

According to the Commission, there are therefore objective reasons which explain

why the system of protection against unfair dismissal should apply only to undertakings other than small undertakings; they are able to continue to employ an employee whose dismissal is not socially justified. The Commission therefore considers that the exclusion of small businesses from the ambit of a system of protection against unfair dismissal does not constitute aid within the meaning of Article 92 of the Treaty. It is consequently unnecessary, according to the Commission, to decide whether that exclusion distorts competition and whether trade between the Member States is affected.

In the light of the foregoing, the Commission proposes the following answer to the first question submitted by the national court:

'The exclusion of small businesses from the ambit of the system of protection against unfair dismissal under the second sentence of Paragraph 23(1) of the Law on unfair dismissal (in its consolidated version of 25 August 1969, as amended by the first Law on the revision of labour law) is compatible with Article 92(1) of the EEC Treaty.'

The second question

The *German Government* points out that national legislation entails indirect discrimination against women where, although its wording is neutral, that legislation affects more women than men adversely, unless that difference in treatment is justified by objective factors unrelated to any discrimination on grounds of sex (see the judgment in Case C-184/89 *Nimz* v *Freie und Hansestadt Hamburg* [1991] ECR I-297). According to the German Government, the third sentence of Paragraph 23(1) of the Law on unfair dismissal does not entail any discrimination against female employees.

The German Government states first of all that the third sentence of Paragraph 23(1) of the Law on unfair dismissal encourages the creation of part-time jobs. The fact that part-time workers are not taken into account in calculating the number of employees under the second sentence of Paragraph 23(1) of the Law on unfair dismissal allows undertakings with five full-time employees to increase their workforce if necessary by employing part-time workers, without coming within the ambit of the system of protection against unfair dismissal.

The German Government goes on to stress that the applicability of the system of protection against unfair dismissal to a given employee does not depend on the question whether the working hours of that employee exceeds the threshold in the third sentence of Paragraph 23(1) of the Law on unfair dismissal. Whatever his own working hours, an employee is or is not protected against unfair dismissal by the Law on unfair dismissal according to whether or not the undertaking he works for has more than five employees whose working hours exceed the threshold in the third sentence of Paragraph 23(1) of the Law on unfair dismissal.

In the opinion of the German Government the third sentence of Paragraph 23(1) of the Law on unfair dismissal could result in discrimination against women if the undertakings which fall outside the ambit of the Law

on unfair dismissal because of the provisions in the third sentence of Paragraph 23(1) employed more women than men. The German Government states, however, that there are no statistics available on the number of part-time workers, and how many of those employees are men and how many are women, in undertakings employing more than five workers (regardless of the working hours of those five workers). The only figures available show that in 1987 undertakings employing between 5 and 9 workers employed approximately the same number of female (1 612 067) as male workers (1 578 919).

Accordingly, the German Government proposes that the Court reply in the negative to the second question from the national court.

As a preliminary point the *Commission* states that the discrimination which the Law on unfair dismissal is said to entail relates to the protection of workers against unfair dismissal, not workers' pay. It considers, however, that, in view of the fundamental importance Community law gives to the principle of equal treatment the case law of the Court concerning the prohibition of all forms of indirect discrimination in relation to pay laid down in Article 119 of the Treaty may be transposed to the prohibition on all forms of discrimination in the conditions governing dismissal provided for in Article 5(1) of Directive 76/207. Nevertheless, the Commission points out that although that provision was held to have direct effect in the judgment in Case 152/84 *Marshall* v *Southampton and South-West Hampshire Health Authority* [1986] ECR 723, the provisions of a directive have never been held to have horizontal direct effect. Accordingly, the Commission considers that in any event the plaintiff in the main proceedings may not rely on the possible incompatibility of Paragraph 23(1) of the Law on unfair dismissal with Article 5(1) of Directive 76/207.

Since it nevertheless takes the view that in the present case it is for the national court to determine the relevance of the second question to the settlement of the dispute before it, the Commission considers it necessary to take a position on that question.

According to the Commission, Paragraph 23(1) of the Law on unfair dismissal does not, correctly speaking, place part-time workers at a disadvantage in relation to other workers. As proof of that the Commission points out that in the present case the plaintiff in the main proceedings does not benefit from protection against unfair dismissal even though her working hours exceed the minimum threshold provided for in the third sentence of Paragraph 23(1) of the Law on unfair dismissal.

However, Paragraph 23(1) of the Law on unfair dismissal establishes a difference in the treatment of two categories of workers. Whereas workers employed in small businesses are not protected against unfair dismissal, workers employed in other undertakings benefit from such protection. Accordingly, the system established by Paragraph 23(1) of the Law on unfair dismissal could entail discrimination against women contrary to Article 5(1) of Directive 76/207 if small businesses employ more women than men. The Commission considers that, in accordance with the case law of

the Court, it is for the national court to decide whether that is in fact the case (see in particular the judgment in Case 170/84 *Bilka* v *Weber von Hartz* [1986] ECR 1607).

The Commission points out, moreover, that, if the system established by the Law on unfair dismissal does treat men and women differently, it is necessary to consider whether or not that difference of treatment is justified by objective factors which exclude all discrimination on grounds of sex. Referring to the judgment in Case 171/88 *Rinner-Kühn* v *FWW Spezial-Gebäudereinigung* [1989] ECR 2743, the Commission states that it is for the national court to consider that question.

Accordingly, the Commission proposes that the Court answer the second question referred by the national court as follows:

'The provisions of Paragraph 23(1) of the Law on unfair dismissal constitute indirect discrimination against women contrary to Article 5(1) of Directive 76/207/EEC if their effect is to exclude many more women than men from general protection against unfair dismissal, unless the State in question can demonstrate that that provision is justified by objective factors unrelated to any discrimination on grounds of sex. A woman affected by such discrimination may not, however, rely on the direct effect of the directive in relation to a private employer.'

III — Replies to questions put by the Court

The Court asked the German Government to give:

1. the total number of male workers and the total number of female workers employed in the Federal Republic of Germany;

2. the total number of male workers and the total number of female workers employed in the Federal Republic of Germany by undertakings which are excluded from the field of application of the Law on unfair dismissal, that is, undertakings which employ at most five workers whose working hours exceed 10 hours per week or 45 hours per month;

3. for the undertakings under point 2 above, the total number of male workers and the total number of female workers whose working hours exceed 10 hours per week or 45 hours per month (including full-time workers);

4. for the undertakings under point 2, the total number of male workers and the total number of female workers whose working hours are fewer than 10 hours per week or 45 hours per month.

In answer to the *first question*, the German Government pointed out that, out of 26 176 000 workers employed in the Federal Republic of Germany in April 1990, 15 543 000 workers (59.38%) were male workers. The number of female workers was 10 633 000 (40.62% of the total number of workers). At that time, 1 617 000 workers worked fewer than 10 hours per week. Out of those workers, 704 000 were male while 913 were female.

With regard to the *second*, *third*, and *fourth questions*, the German Government pointed out that the existing figures did not include data with respect to undertakings which did not come under the Law on unfair dismissal. The statistics for 1987 supplied only the following information (the number of undertakings and the number of workers are in thousands):

Undertakings		Number of workers			
Work force	Number	Men		Women	
		Total	Part-time	Total	Part-time
1 — 4 workers	1 688	2 608 75.0%	201	854 25.0%	551
5 — 9 workers	495	1 579 49.5%	182	1 612 50.5%	627
More than 9 workers	398	11 995 59.1%	520	8 311 40.9%	2 323
Total	2 581	16 182 60%	903	10 777 40%	3 501

J. L. Murray
Judge-Rapporteur