

## SHAM CONTRACTS IN THE FIELD OF HEALTH CARE

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**ABSTRACT:** *In this paper we introduce the employment contracts, which shall be deemed as sham contracts in the field of healthcare. According to the Hungarian Civil Code contracting parties have the right to freedom of contract, which means, that they are allowed to conclude contracts and to choose the other party freely and to determine the content of the contract freely. This provision is the so-called freedom of contract. This principle can not be applied to such contractual relationships, where the parties would like to cover up their real legal relationship with another contract. These kinds of contracts are sham contracts. Sham contracts are null and void. Such contracts can be concluded if the parties are intended to get some kinds of legal or economical benefit in an illegal way, or they want to circumvent a disadvantageous legal situation. These kinds of sham contracts can be found in some special employment relationships, e.g. in the field of healthcare.*

**KEYWORDS:** *sham contracts, civil law, labour law, working activity, healthcare system, Hungarian Civil Code, Hungarian Labour Code*

**JEL CODE:** *K0*

### 1. INTRODUCTION

Activities pertaining to working can be executed in various kinds of legal relationships. According to the principle of freedom of contract, parties can agree freely about the type of their concluding contract for the interest of mutual working. There are some kinds of works, which can be executed only in a framework, which is defined by the law. *Healthcare activity is such an activity*, because Act LXXXIV of 2003 on certain aspects of healthcare activity *contains a detailed list* about the types of contractual relations.

According to this list, healthcare activity can be executed within the framework of:

- liberal profession,
- sole healthcare entrepreneur,
- member of a collective enterprise,
- public servant,

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- civil servant,
- employment,
- ecclesiastic,
- voluntary and
- as a member of a sole proprietorship relationship.

In certain cases, some of the abovementioned legal situations, which are aiming at working is carried out *within the framework of a personal service contract* (e.g. liberal profession or sole healthcare enterprise), but in some other cases the *working situation is realized by an employment contract* (e.g. employment).

The possibility of choice is much narrower in such case, where the medical employees don't have any professional qualification, because they cannot enter into a legal relationship within the framework of a liberal profession, additionally they cannot fulfill any healthcare work neither as a sole healthcare enterprise nor as member of a sole proprietorship. (DÓSA - KOVÁCSY 2011, p. 750)

## 2. ABOUT THE SHAM CONTRACTS IN GENERAL

The part of freedom of contract, which is concerning to the choice of the type of contract is allowed to the contracting parties only in the case, if their underlying contract of the activity pertaining to working allows them this freedom. In such cases, where the working activity incorporates the features and attributes of a concrete relationship, especially the characteristics of an employment relationship, parties are not entitled to conclude the contract contrary to the employment relationship and cannot agree upon the rules of the general civil law and conclude for instance a personal service contract. In a concrete case, the Supreme Court declared the followings: In the case if the content of the contract concluded by the employer and individuals should be regarded an employment relationship; the legal relationship couldn't be subtracted from the rules of employment relationship even if the will of the parties pertaining to this neither. The legal reason of this decision is that, the principle of freedom of contract is concerning only to the definition of the content of the contract and not to the denomination of the contract.<sup>1</sup> According to the Act V of 2013 on Hungarian Civil Code (henceforward abbreviated: HCC) *sham contracts shall be null and void* and if such contract is intended to disguise another contract, the rights and obligations of the parties need to be adjudged on the basis of the disguised contract.<sup>2</sup>

Generally, sham contracts are concluded if the parties are intended to get some kinds of legal or economical benefit in an illegal way, or they want to circumvent a disadvantageous or unfavorable legal situation (CSEHI 2014, p. 57). Simulation is a

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<sup>1</sup>BH 2003. 432.

<sup>2</sup>Section 2 of Article 6:923 of Hungarian Civil Code.

*bilateral and deliberating behavior*, when the common will of the parties is concerning to the concluding contract, which would come into being upon their legal statement, would not be concluded or would be concluded with a different content and different legal consequence.<sup>3</sup> In the case if sham contract is regarding to a working activity, contracting parties would like to make the impression that they concluded a civil law contract, typically a personal service contract.<sup>4</sup>

Freedom of the type of contracts does not mean that the real and relevant content of the legal relationship is based on a civil law contract come up against the essential features of the type of the contract chosen by the parties. If the parties' real legal relationship is different than their named legal relationship, the concluded contract is a sham contract; therefore it is null and void.

In this case the contract and the legal relationship shall be adjudged on the basis of the disguised contract, here, in the concrete case upon the employment contract. According to the judicial practice, the nature of the work what needs to be performed doesn't disqualify the establishment of a civil law styled legal relationship (e.g. service contract). The most important question is the domination of the elements of the civil law relationship, not the nomination of the parties' contract in the judgment of the nature of the concluded legal relationship. In this way, the activity of a doctor who executes his task in the framework of a service styled contribution contract have to be considered an employment relationship if his activity is realizing under the circumstances of employment relationship (e.g. on the hospital department and with the means of the principal, by the instructions, circular mails, information, regulations of the principal).

### **3. SHAM CIVIL LAW CONTRACTS, AND HIDDEN EMPLOYMENT CONTRACTS IN THE FIELD OF HEALTHCARE**

Civil law contracts appeared in the area of healthcare services, especially in the case of on-call duty, first when the *Directive 2003/88/EC of the European Parliament and of the Council concerning to certain aspects of the organization of working time* came into force.

- On the one hand, the reason of this tendency is that, the restrictions shall not been applied in a civil law contract which are regarding to the working-time and rest period (such as the regulations of termination and severance pay), and
- On the other hand, healthcare providers can provide a favorably remuneration to the workers on the basis of a civil law contract. Most of the contracts are concluded by the consensus of the parties, but the examination of sham contracts became necessary, especially if a service contract is intended to disguise an employment contract.

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<sup>3</sup>BH 2001. 29.

<sup>4</sup>BDT 2005. 1123.

*Outpatient service* is another appearance of sham contracts in the field of healthcare, where the employee and the sole entrepreneur doctor execute the same type of work by different legal relationships. It also occurs in the outpatient services that the very similar work is executed by doctors, upon an employment and individual or associated enterprises relations. This situation means, that the work is based on different legal relationships, and it also brings up the question of sham contract.

#### **4. DELIMITATION OF LEGAL RELATIONSHIPS AIMING AT WORKING**

Until 2012, the typical features and attributes which are concerning to the employment relationships were determined by a directive<sup>5</sup>, and these aspects are still influential nowadays too.

According to these attributes it can be separated that the legal relationship aiming at working activity, has the typical features and attributes of a *civil law contract or an employment contract*. The existence of employment relationship can be stated, if the consensus of parties aiming at conclusion of civil law contract, because even the unanimous will of the parties cannot pull out the working activity from the effect of labour law.

Consequently, the contracting parties' will is significant only in the case if the feature of the activity allows the choice of the type of contract. In such case we shall focus on the circumstance, whether the parties' presumed intent is aiming at the concluded contract. In this case, statements of the contracting process and of the working activity are particularly relevant. Such a statement is for example the employee's demand for the employment contract, but he needs to accept a personal service or a professional service contract in order to the possibility of employment would remain for him.

##### *1. Subject of the contracts, feature of the activity*

In case of an employment relationship, the tasks and the activities are determined by the *scope of duties* of the employee. The most important attributes of the task in the employment relationship are *continuity, regularity and periodicity*. In general, employee doesn't enter such an employment relation, where he needs to fulfill a concrete task or achieve the result with working activity, but he needs to fulfill his job and scope of duties continually. The scope of duties of his job is determined by the employer day by day, this situation presumes a hierarchical relation between the employer and the employee. The scope of duties, as a sum of activities, is a strange definition in the system of civil law, because service contract or contract for professional services are relating to concrete tasks, orders, or services. In the case if the individual's task is based on a civil law contract actually means a sum of activities of a concrete job position, the legal relationship between the parties result an employment contract. It is strange from the civil law as well,

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<sup>5</sup>7001/2005. (MK170.) FMM-PM Directive

that the worker – under certain circumstances defined by law – *could be obliged unilaterally* for the kinds of activities which aren't in the contract. In the case if the working activity is based on the regulations of civil law the parties are allowed to diverge from the content of the contract only by consensus.

To work under the regulations of civil law is an *ad hoc activity*, which mostly occurs in irregular ways, but appears as an activity on defined times.

On the contrary the task's job characteristic and its' regularity are tending to the employment relationship.

The so-called *employment in a double relationship* is realized often if the employee works on the medical on-call duty. In such cases, the employer employs the doctor for the same tasks in the framework of an employment relationship for the time of the daily work time (public servant relationship) and in the time of the on-call duty the relationship is based on a personal service contract. The latter contract shall be deemed a sham contract, because the actual will of the contracting parties is tending to an employment relationship which is disguised by a civil law contract. So if the *medical worker's job profile contains* the obligation of on-call duty, than this task cannot be the subject of an assignment contract with the same medical worker.

It can be the situation especially in the case if the employment and civil law contracts are presented in the same time for the execution of the same task. For example if the on-call duty is executed on the same hospital grade, upon an employment relationship and upon an agency contract by the same doctor (DÓSA - KOVÁCSY 2011, p. 828).

For a similar reason the family doctor, who operates his praxis within the framework of enterprise, isn't entitled to conclude a professional service contract with the nurse for the circumvention of some constraints resulting from the employment relationship (e.g. working time). If the work of the nurse connects to a certain workplace and she gets constant pay for her continuous and regular work, than this medical work is based on an employment relationship, so it cannot be deemed a professional service contract, because this would be a sham contract.

## 2. *Duty of personal working*

According to the regulations of Civil Code, within the framework of personal service contract and work contracts, the parties *can employ other persons (such as assignments and agents)* to fulfill their civil law obligations. According to this, if the doctor is employed as a sole healthcare entrepreneur by the municipality under a personal service contract, the doctor has to ensure his replacement by himself. Under an employment relationship the employee cannot fulfill his obligations by an assistant. An employee needs to perform his task personally; he is not entitled to demand an assistant. Although if a contract contains the requisition of a substitute, assistance or subcontractor, it does not necessary confirm that the working activity happens within the framework of the civil law. The duty of personal working could appear in the working situations, which are based on the regulations of civil law.

The person of the doctor could be really dominant, especially if he is a family doctor or specialist in pediatrics, so the requisition of third parties for the performance can be allowed only in special cases.

### 3. *The employer's duty on employment*

In case of an employment relationship, employer has to provide a work for the employee during the time of the employment relationship, while the obligation of employee has to be available continuously at the time and in the place of the work. It is such a general obligation which is unknown in the area of civil law. The most important and essential obligation in the civil law relationships relating to working activity is the providing of the contractual service and creating some other result by work. On the contrary, according to the labour law the most important obligation is to being available for the employer; the failure or imprecise performance of this obligation has some serious legal consequences.

### 4. *Hierarchical relationship*

Medical workers have to fulfill their tasks under an employment contract and *in the healthcare service of the employer*, so hierarchical relationship in their situation is common. The hierarchical relationship is regulated by the employer's own organizational rules (e.g. organizational and operational regulations). Accordingly the employee executes his tasks as a member of a certain department, but he also exercises the employer's rights on the other stages; for instance the chief medical officer executes these rights above the other doctors and employers. If it could be determined, that the working doctor is entitled to exercise employer rights, on the foregoing of the labour or tax control, than this circumstance confirms the existence of an employment relationship.

The relationship between the employee and the employer is *a strict hierarchical relation*, which demonstrates the employer's unilateral right to instructions. On the contrary, in the case of a civil law relationship parties conclude their contract in a coordinate relation and *on the basis of the principle of interdependence*. The judicial practice is unified in the question, that if a legal relationship has a hierarchical characteristic it cannot be deemed as a service contract, but it is an employment relationship.<sup>6</sup> The legal relationship cannot be reclassified to an employment relationship without the hierarchical characteristic and the wide range of the right to give instructions.<sup>7</sup>

### 5. *Issues of right to instruction and right to control*

The employee has to fulfill his job *upon the guidance and instructions of the employer* because of the hierarchical relation. The employer is entitled to control the execution of his instruction fully and in details.<sup>8</sup> The rights to instruction and right to control are not only applied in an employment relationship, but in service contracts and contracts for professional services as well. The agent shall follow the instructions of the principal.

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<sup>6</sup>EBH 2002. 677.

<sup>7</sup>EBH 2003. 981.

<sup>8</sup>Section 2 of Article 42 of Labor Code

Instructions cannot be given for the organization of work and they cannot render the performance more burdensome.<sup>9</sup> The customer can check the work and the used materials at any time.<sup>10</sup> The agent needs to follow the instructions of the principal as well. The agent may disobey the principal's instruction if it is essential for the principal's interest, and the principal cannot be notified in advance. In such a case the principal shall be notified without delay. All costs of the agent incurred in connection with the fulfillment of the instruction shall be reimbursed by the principal.<sup>11</sup>

In the case of an employment relationship the instructions can be applied for all the phases and elements of the working activity, but in the framework of the personal and professional service contract, instructions are concerning only to the result or the service and not to the details of the working activity.

According to the judicial practice, the employer cannot refer to a personal service contract between the parties, if they agreed all of the elements of the employment relationship.<sup>12</sup> The Supreme Court made a decision in a similar case, when a sham personal service contract aimed at the circumventing of the rules of overwork. The Court declared that the worker produced the task not upon his own discretion, but under the detailed instructions of the principal. The Supreme Court declared in another case, that the right of instruction cannot be deemed a qualifier attribute by itself. *„If the worker fulfills his tasks within the framework of a personal service contract, this relationship cannot be deemed employment relationship, even if he had to work by the instructions of the employer, because personal service contract shall be performed by the principal's instructions.”*<sup>13</sup>

#### 6. Determination of the working time and the place of work

In case of an employment relationship, *a duration of the working, the duty list of the working, the schedule of the work time are determined by the employer*, but within the boundaries of the regulations of Labour Code. In case of a civil law contracts, the principal is entitled to determine only the deadline or the cut-off date of the execution of the task. The working time is not scheduled; because the needed time for fulfilling the task is determined by the contractor. This is the reason, why the determination of the working time or the scheduling of this is not a decisive attribute.

The essential element of the employment contract is the *definition of the workplace*. The workplace of the employee shall be defined in the employment contract.<sup>14</sup> According to a professional service contract and a personal service contract, the obligor is entitled to choose the place of the performance by himself. In this way some activities under personal or professional service contracts are localized (e.g. hospital, clinic, home of the

<sup>9</sup>Section 1 of Article 6:240 of Hungarian Civil Code

<sup>10</sup>Section 1 of Article 6:242 of Hungarian Civil Code

<sup>11</sup>Section 1-3 of Article 6:273 of Hungarian Civil Code

<sup>12</sup>BH 2001. 445.

<sup>13</sup>BH 1992. 736

<sup>14</sup>Section 3 of Article 45. of Labor Code

patient, or the family doctor's clinic). At the same time some percent of activities need to be fulfilled by the framework of employment relationship can be executed at the place defined by the employer (e.g. telemedicine).

7. *The providing of means, resources, and safe work conditions for the employment in order to working*

Doctors and professionals, who work in employment relationship, use the means of the healthcare service provider. On the contrary, an assignment doctor uses his own materials for the fulfillment of his work. This feature is not conclusive, because on the one hand the real owner of the office and the used material of an entrepreneur doctor is the municipality; on the other hand employee could use his own materials and means for the working. In a relationship, which is based on civil law contract, the dentist can account the costs of means, and used materials in his pay rate, while this process does not appear in an employment relationship.

*The responsibility for the implementation of occupational safety and occupational health requirements lies on the employers.* In the case of a personal and a professional service contract, the responsibility of medical employee is concerning to provide his own safe work conditions.

The Article 14 of the *Act CXLVII of 2012 on the Fixed-Rate Tax of Low Tax – Bracket Enterprises and on Small Business Tax* contains concrete standpoints about the delimitation of employment relationship. According to this, contracts, transactions and other similar operations concluded by low tax-bracket enterprises shall be judged upon their true content and under the principle of due course of the law. If a concluded agreement or transaction with the low tax-bracket enterprise is construed, based on its contents, to *disguise an employment relationship* between the low tax-bracket entrepreneur and a third party, the legal consequences relating to taxation shall be determined on the basis of employment regulations.

According to the Act, within the framework of a control procedure, the tax authority shall presume – pending proof to the contrary – which the low tax-bracket entrepreneur has entered into an employment relationship with a third party. *The presumption shall be deemed rebutted if more than one of the following factors realizes:*

- a) the low tax-bracket entrepreneur did not solely carry out the activities by himself
- b) the low tax-bracket entrepreneur didn't obtained at least 50 per cent of his income for the calendar year from the same third party
- c) the third party contracted with the low tax-bracket entrepreneur could not have given instructions to the means of carrying out the activity;
- d) the place where the activities are carried out is owned by the low tax-bracket entrepreneur;
- e) the means and materials for carrying out the activity has been supplied to the low tax-bracket entrepreneur by someone other than the contracting third party;
- f) the order of the activity has been arranged by the low tax-bracket entrepreneur.

## 5. LEGAL ADJUDICATION OF ASSIGNMENT CONTRACTS

As it was mentioned before, assignment contracts have an increasing importance in the field of healthcare. These kinds of contracts could be concluded by such medical workers, or organizations, who provide the healthcare service *directly*, by the profession of the department of certain healthcare service provider (principal) *personally, or with their medical employees*, and *in the name of the principal healthcare service provider* for the patients of the principal healthcare-service provider. Further important criterion is also, that the necessary factual and personal conditions for the work need to be provided by the assignment.<sup>15</sup>

*In a case of the personal cooperation* the person or organization take part in the provision of healthcare service shall provide only the personal conditions under the assistance contract concluded by the parties. The existence of the material conditions have to be provided by the healthcare servicer.<sup>16</sup>

The principal healthcare service provider has no obligation to the pre-payment of tax or payment of the contribution from the invoiced revenue of the assignment healthcare service provider. With this sum of money the assignment healthcare service provider disposes freely. In most cases the sole healthcare entrepreneur doctor, or the doctor, who is a member of a collective enterprise can be deemed an assignment healthcare service provider. In connection with the content of the contract it is need to be analyzed, whether the parties defined the place of work, the working time of the doctor, or the instruction right of the principal, or they didn't.

## 6. LEGAL CONSEQUENCE OF SHAM CONTRACTS

Contracts, which are the basis of working activities, are adjudicated by the *administrative and labour courts*. On the basis of the decision the court is entitled to reclassify the existing contractual relationship into an employment relationship. The content of the contracts can be analyzed by the tax authority and the employment inspector as well.

The Act LXXV of 1996 on labour inspection declares that the employment authority is entitled to classify the employer and his workers relationship under the monitoring process. For this, the employer needs to provide all the evidences, on the basis of which it can be classified that the basis of the certain work is a civil law contract, an employment contract, or the work is managing without any consideration.<sup>17</sup> If the authority states that the parties' civil law contract is actually disguise an employment contract, the contract will be reclassified into an employment contract since the first day of the working activity and it monitors that the regulations of employment relationship would have been

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<sup>15</sup> Point k) of Article 2 of 96/2003. (VII. 15.) Government Decree on General conditions of healthcare services and on operational proceeding

<sup>16</sup> Point n) of Article 2 of 96/2003. (VII. 15.) Government Decree on General conditions of healthcare services and on operational proceeding

<sup>17</sup> Section 5 of Article 1 of the Act LXXV of 1996. on labour inspections

observance since the first day of the work. Accordingly, the employer could be committed with a back payment obligation for the worker and because the employee is an insured person, the employer shall pay the social security taxes of the worker as well. Additionally, the employment authority *can impose labour fine* as well.

The employer medical service provider can be obliged by the employment authority to notify the reclassified employment relationship to the tax authority.

*The tax authority cannot* infringe the contracting autonomy of the parties; hereby it cannot convert the sham civil law contract into an employment contract. On the contrary, the tax authority has the right to judge the contracting relationship of the parties as an employment contract and determine the outstanding taxes and contributions in the way, if the civil law contract would be an employment contract. This kind of situation eventuates not only the imposition of tax arrears, but the default of tax penalty or penalty for absence too. Fiscal relations and civil law relations are different from each other and the statement of tax authority doesn't have any affection to the parties' civil law relation. The classification of the tax authority is relevant only in the fiscal point of view and it has no effect for third parties.<sup>18</sup>

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