CLIFFORD GOULDSON
LAWYERS

Contractors | The Risk of Misclassification: Are advisors at risk?

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1. Introduction | Engaging Contractors

1.1 When we think of 'workers' we typically think of employees. This relationship is by far the most common within the workplace and generally way to hire.

1.2 But sometimes, for whatever reason, a business may to find themselves in a situation where they are considering whether it is more beneficial to outsource a particular kind of work to an independent contractor.

1.3 This in itself is fine, but not a decision that should be made with blind confidence. Engaging a worker correctly can be tough and doing it incorrectly can lead to disaster.

1.4 Indeed, the more a contractor looks and works like an employee, the higher the chances are that the worker would be deemed by a court to *be* an employee.

1.5 The issue with this lies in the fact that it can be very challenging to structure a relationship in a way that confirms an individual's status as a contractor with certainty.

1.6 There is not a single agreed definition of what a contractor is and instead it is a matter of interpretation for the courts.

1.7 What we are now left with is an approach that is deeply-rooted in the common law, that is fraught with '*ambiguity, inconsistency and contradiction*[1]'.

1.8 From an advisor's perspective, it is critical to understand that characterising a worker's status requires one to consider many different issues and that incorrect advice can lead to advisors themselves receiving penalties for their client's contraventions.

2. Distinguishing Employees From Contractors

2.1 Vicarious liability of employers

(a) The modern distinction between employee and independent contractor is primarily drawn from the development of the common law doctrine of vicarious liability.

(b) It is generally the position that an organisation may be vicariously liable for the wrongful acts or omissions of its employees but not any independent contractors it may engage.

(c) An example of how this operates is in the case of *Sweeney v Boylan Nominees*[2], where a lady was injured at a service station after she opened the door of a fridge which came loose and struck her:

(i) following her injury, the lady sued the refrigeration company which was contracted by the service station to maintain the fridge; and

(ii) the refrigeration company avoided liability for the injury as it had arranged for an independent mechanic to repair the door, who the court determined was an independent contractor and not an employee of the company; and

(iii) had the court determined that in actuality the mechanic was an employee of the refrigeration company, then it may have been likely that the company would have been held vicariously liable for the actions of the mechanic.

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[1] *Construction, Forestry, Maritime, Mining and Energy Union v Personnel Contracting Pty Ltd* [2020] FCAFC 122

[2] [2006] HCA 19; (2006) 226 CLR 161

(d) For the most part, the court is unwilling to extend this sort of liability to contractors lightly[3], which can be one of the reasons why engaging a contractor is desirable. But it is important to note that this not true in every case and a few challenges to this in the past have achieved success[4], such as where there is a duty to ensure that a general system of work is safe.

(e) Such a duty is known as a non-delegable duty, and an example of this can be found within the *Work Health and Safety Act* 2011 (Qld) where an employer is required to provide a safe workplace to all persons on that workplace including employees and contractors.

2.2 Multi-factor test

(a) How the courts determine who is an who is not an employee is not only used to determine liability in cases of negligence, but also used to determine the applicability of certain statutory provisions such as those within the Fair Work Act 2009 (Cth) (**FW Act**).

(b) The reason for this is that FW Act, for the most part, provides (rather unhelpfully) that the term 'employee' for the purposes of most entitlements under the FW Act has its ordinary meaning. In other words, this means that the term is determined by the common law and how the courts view the relationship.

(c) In the past, the courts traditionally looked to the element of control as the determinative factor in establishing a worker's status. A person was normally seen as an employee where they were subject to the command of their master as to the manner in which they were to perform the work.

(d) However, this definitive approach has now evolved into a more sophisticated multi-factorial approach which requires an assessment of the 'totality of the relationship'.

(e) A big part of this, is the idea that there is no exhaustive list of relevant factors that can be ticked off or identified that provide certainty on a worker's status.

(f) Nevertheless, the case law has provided a list of consistent examples of 'indicia' which are usually considered. These are as follows:

Issue	Test	Employee	Contractor
Control	Is the employer given the right of control over the other party, and is this control exercised?	Yes	No
How the work is paid for	Does the contractor submit an invoice on completion of task?	No	Yes
How is the contract determined?	Does the contract provide for termination by x number of weeks' notice or payment in lieu?	Yes	No
Individual or broader legal entity party to contract	Is the legal entity employed to do the work a partnership or company?	No	Yes
Provision and maintenance of equipment	Do the contractors provide their own tools and cover the cost of repair?	No	Yes
Hours of work	Are hours set for attendance on site?	Yes	No
Leave	Is leave paid?	Yes	No
Taxation	Is PAYE tax paid?	Yes	No
Capacity to select own employees and delegate	Can work be delegated at the contractor's discretion to employees	No	Yes

[3] *Leichhardt Municipal Council v Montgomery* [2007] HCA 6

[4] *Hossain v Unity Grammar College Limited & Ors* [2019] NSWSC 1313

Issue	Test	Employee	Contractor
	of contractor's choice		
Risk – capital investment	Is the contractor exposed to a loss of capital investment in the contract?	No	Yes
Superannuation	Are superannuation contributions being made?	Yes	No
Other jobs	Is the person free to carry on other jobs at the same time?	No	Yes
Organisation	Is the person interwoven or considered part of the organisation?	Yes	No
Professional indemnity (PI)	Does the contractor carry his or her own PI insurance?	No	Yes

(g) It is ultimately a question of overall impression which is gained by balancing the above indicators (among others) in contemplation of the specifics to the case at hand.

(h) Without a thorough understanding of how the courts treat these indicia depending on the case, it can be difficult to hold confidence about a worker's status. The following excerpt from a 2008 case[5] puts it rather succinctly:

> *'[when] a relationship depends upon various indicia, there is always a danger in extracting one indicium and giving it decisive weight because of the way in which it has been used in a different context, rather than weighing each matter in the balance'.*

(i) In fact, this year alone two decisions of the Full Federal Court have demonstrated just how difficult and sometimes contradictory this process can be.

2.3 Personnel Case

(a) In CFMMEU v Personnel Contracting Pty Ltd[6] (**Personnel Case**) the Full Federal Court expressed some frustration around how it was bound by previous decisions after it concluded that, despite compelling evidence to the contrary, a 22 year old British backpacker was an independent contractor of a labour hire company.

(b) The facts of the case concerned the employment status of a young man, Mr McCourt, who worked as a general labourer for a labour hire company on construction sites in Perth under the supervision and control of a builder, Hanssen Pty Ltd.

(c) The question at hand was whether Mr McCourt was an employee of the labour hire company, Personnel Contracting Pty Ltd, which was the contracting entity that provided him with the opportunity for work and paid him for his services.

(d) Mr McCourt applied under the FW Act for orders for compensation and penalties against Personnel based on the allegation that he was not paid or treated in accordance with the relevant modern award, which would have applied had he been correctly engaged as an employee.

(e) Noting the factors set out in the table above, the court identified that there were several matters present in the relationship which indicated an employment relationship:

(i) whilst at work, Mr McCourt was directed what work to do and the way in which it had to be done;

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[5] *Wesfarmers Federation Insurance Ltd v Stephen Wells trading as Wells Plumbing* [2008] NSWCA 186

[6] *Construction, Forestry, Maritime, Mining and Energy Union v Personnel Contracting Pty Ltd* [2020] FCAFC 122

(ii) Mr McCourt supplied basic clothing such as steel cap boots, hard hat and “hi-vis” shirt, but other tools were supplied by Hanssen;

(iii) the majority of the work performed by Mr McCourt was that of a low skilled labourer;

(iv) Mr McCourt was engaged in physically demanding work, around 50 hours per week, which meant that it was not feasible for him to have another job;

(v) Mr McCourt was never told he could delegate the performance of the work assigned to him to a third party;

(vi) Mr McCourt “clocked” on and off, filled in a timesheet, did not keep a record of his hours worked and was never asked to provide any invoice or statement of hours worked;

(vii) if Mr McCourt was ill or running late, he would inform the site manager ahead of time. He also took leave of a few days to go on a short holiday, for which he was required to put in a request for leave with Hanssen.

(f) Chief Justice Allsop in this instance expressed how, if it were not for past decisions, he would have favoured an approach which viewed Mr McCourt as a casual employee of Personnel, when taking into consideration the above circumstances and in particular where it was clear that Mr McCourt:

(i) did not appear to be carrying on his own business;

(ii) had no desire to act as anything but a builder’s labourer; and

(iii) merely sought remuneration in exchange for providing labour.

(g) Notwithstanding that opinion though, at least two other intermediate courts of appeal had applied the established common law principles of contractor distinction and characterised similar relationships between unskilled workers and labour hire companies as being ones of principal and independent contractor, primarily by reference to the terms of the contracts that governed those relationships.

(h) Indeed, some time ago, one of those cases actually dealt with another contractor of Personnel suing the company over a near identical contract for very similar reasons. In that case, it was found that the worker was an independent contractor.

(i) The primary issue here was that in tripartite labour hire arrangements, there is no contractual arrangement between the worker and the person who requires the labour; rather the contractual relationship is between the worker and the labour hire agency or provider, which means that significant weight must be given to the contractual terms between those parties, which of course were carefully written to present the relationship as one of principal and contractor.

(j) The judge also said that there were problems with the court to depart from earlier similar decisions, because:

(i) those past decisions were based on a long line of common law authority and upon having those decisions become part of the common law, had informed other decisions of courts;

(ii) Personnel and other similar enterprises had relied on those decisions to develop their businesses over a substantial period of time; and

(iii) stigmatising these types of arrangements would lead to numerous civil penalties and severely disrupt the industry.

(k) Importantly, the intermediate appellate courts are not permitted to depart from decisions of other intermediate appellate courts in other jurisdictions on the interpretation of Commonwealth legislation unless they are convinced that the interpretation is plainly wrong - which in the Personnel Case was not so.

(l) The decision demonstrates the frustration that is inherent with the binary level of inquiry that the court is currently stuck with in the interpretation of these types of relationships.

(m) It also goes to show how important it is to have contracts correctly drafted within the context of a particular circumstance.

(n) The case demonstrates that experience and knowledge in characterising a relationship is critical because despite an overwhelming number of elements that may point to an certain relationship the characterisation is one that is deeply ingrained within the case law.

2.4 Truck Drivers Case

(a) In another Full Federal Court decision this year[7], in the case of Jamsek v ZG Operations Australia Pty Ltd, two truck drivers each engaged for 35 years as independent contractors were found to have in fact been employees all along.

(b) In reaching this conclusion, the court applied the same multi-factor approach however, within this case placing significant emphasis on the degree of control and independence required for a worker to be classified as a bona fide contractor.

(c) Indeed, the truck drivers had many features of independent contractors. For example, they had:

(i) invested heavily in their trucks;

(ii) a level of control over how they organised their work, including organising their own runs and distributing the deliveries between themselves;

(iii) set themselves up in the usual fashion of contractors, whereby they were party to a series of agreements over the years that described them as contract carriers, they were organised as partnerships, remitted GST and claimed input tax credits and split income with their wives;

(iv) the ability to delegate their work and had on at least one occasion arranged for a substitute driver; and

(v) significant opportunity to increase (or decrease) profitability, through their choice of vehicle, how they organised their runs, finance options and so on.

(d) When looked at based on these points alone, the workers could appear as independent contractors.

(e) However, the court was of the view that reality of the situation was that, aside from the men taking on the risk and expense of owning and operating delivery trucks, they '*certainly had no real independence'*.

(f) While they had some flexibility in the way they carried out their work, they had no real or effective control in respect of the key aspects of the work relationship.

(g) The employing entity effectively dictated:

(i) the hours during which the men were to be available for work;

(ii) what they were to do;

(iii) the remuneration that they were to receive;

(iv) the annual leave that they could take;

(v) the uniforms they were to wear; and

[7] *Jamsek v ZG Operations Australia Pty Ltd* [2020] FCAFC 1934

(vi) the logos that they were to adorn upon their trucks.

(h) Chiefly, the facts of the case indicated that the truck drivers were an integral part of the company's business which of course affected the manner in which all of the relevant circumstances of their relationship needed be considered under the multi-factor test.

(i) The case again demonstrates the importance of looking at the totality of the relationship, rather than cherry picking factors that suit and how important is to continually assess these relationships with guidance from an experienced advisor.

(j) Just because a working relationship has worked in a certain way for a long period of time without hiccup does not guarantee that it will continue in that fashion forever.

3. Deeming provisions

EVEN THOUGH A WORKER MAY NOT BE CLASSIFIED AS AN EMPLOYEE UNDER THE COMMON LAW MULTI-FACTOR TEST, A STATUTORY SCHEME MAY CONTAIN PROVISIONS THAT DEEM CERTAIN TYPES OF WORKERS AS EMPLOYEES.

THERE ARE DIFFERENT REASONS FOR THIS, BUT GENERALLY THEY REFLECT A VIEW THAT A PARTICULAR TYPE OF WORKER SHOULD BE TREATED AS AN EMPLOYEE WITHIN THE PARTICULAR CONTEXT OF THE LEGISLATION.

3.1 Superannuation

(a) One important example of this is the way in which the deeming provisions operate under the *Superannuation Guarantee (Administration) Act* 1992 (Cth) (**Super Act**).

(b) Section 12 of the Super Act provides in part as follows:

> *'Interpretation: employee, employer*
> *(1) Subject to this section, in this Act, employee and employer have their ordinary meaning. However, for the purposes of this Act, subsections (2) to (11):*
> *(a) expand the meaning of those terms; and*
> *(b) make particular provision to avoid doubt as to the status of certain persons.*
> *…*
> *(3) If a person works under a contract that is wholly or principally for the labour of the person, the person is an employee of the other party to the contract'.*

(c) As can be seen, the term employee has its 'ordinary meaning' capturing those who would fall under the common law definition. But subsection 12(3) expands this definition by including any person who works under a contract that is wholly or principally for the person's labour.

(d) Determining who falls under this definition carries with it its own set of rules and tests.

(e) On its most basic reading it could broadly capture a range of unintended agreements, such as that between an advisor and a client, but of course that is not the intention of the legislation.

(f) When considering this very issue in the past, the court considered that, within the context of the legislation, subsection 12(3) of the Super Act was only intended to capture employment-like relationships where work is performed for remuneration, regardless of the fact that the common law might not recognise that relationship as being one of employee and employer[8] .

[8] *On Call Interpreters and Translators Agency Pty Ltd v Federal Commissioner of Taxation (No 3)* [2011] FCA 366 at [306], (2011) 214 FCR 82 at 146 per Bromberg J

(g) A case just last year[9] involved a circumstance where a dentist made a claim against a dental practice, arguing that he should have actually been engaged as an employee rather a contractor and so was entitled to payment for long service leave and superannuation contributions.

(h) Ultimately, he was unsuccessful at demonstrating his status as an employee under the common law (for the purpose of long service leave) due mostly to the level of day to day control that he was free to employ to do his job.

(i) However, where he was successful was in demonstrating that he performed services under a contract 'in an employment-like setting' where the labour component of the contract could have been provided by the dental practice employing an employee.

(j) For further guidance surrounding this, the Australian Tax Office (**ATO**) has published the Superannuation Guarantee Ruling SGR 2005/1 (**Ruling**), which provides detail on a range of worker classification issues, most notably on whether a contract is wholly or principally for a person's labour.

(k) The Ruling states that where the terms of the contract in light of the subsequent conduct of the parties indicate that the individual:

(i) is remunerated (either wholly or principally) for their personal labour and skills;

(ii) must perform the contractual work personally (with no right of delegation); and

(iii) is not paid to achieve a result;

then the contract is considered to be wholly or principally for the labour of the individual and superannuation will therefore be payable.

3.2 Workers Compensation

(a) In certain circumstances a contractor may also be considered a 'worker' under the *Workers' Compensation and Rehabilitation Act 2003* (Qld) (**WCRA**).

(b) As of 1 July 2013 the new definition of 'worker' for the purposes of WorkCover has been in operation. The new definition of 'worker' is:

> *'… a person who works under a contract, and in relation to the work, is an employee for the purposes of assessment for PAYG Withholding under the Taxation Administration Act 1953 Cth (**TAA**) –Schedule 1 Part 2-5*.'

(c) Under Taxation Ruling 2005/16 which deals with PAYG withholding from payments to emplopyees, it sets out the test for when a person will be considered an 'employee' for the purposes of PAYG withholding under the TAA.

(d) According to this Ruling, generally there will be no obligation on an entity to withhold PAYG withholding (and therefore no obligation to take out a Workers' Compensation policy) when the individual:

(i) is paid to achieve a result;

(ii) provides most equipment especially expensive equipment;

(iii) has the power to delegate duties;

(iv) is able to provide services to other businesses; and

(v) has a risk of suffering a financial loss for faulty work.

[9] *Moffet v Dental Corporation Pty Ltd* [2019] FCA 344

(e) An employing entity will likely have to pay Workers' Compensation premiums any individual that falls outside this indicia (including an individual engaged as a contractor).

(f) The definition does not represent a major departure from the multi-factor test, but it is a little clearer with who is a worker for the purposes of workers' compensation.

4. Advice given around contractors

4.1 Drafting the right kind of contract

(a) To draft an appropriate contractor agreement, it is important to incorporate as many factors that point away from an employment relationship, such as (amongst other things):

(i) downplaying any element of control;

(ii) allowing the worker the freedom to work for other clients;

(iii) permitting other workers to assist them;

(iv) having payment occur by results, and on presentation of an invoice;

(v) insisting the that the worker supply their own tools or equipment;

(vi) requiring the worker to insure against any work-related injury; and

(vii) denying the worker any entitlement to paid leave;

(b) It is important to note though, that the actual nature of the relationship and engagement must indicate It is all well and good to have a carefully drafted contract, but as we know, this is not the only aspect that is the court considers when undertaking its multifactor test.

4.2 Sham arrangements

(a) There are situations where in practical or functional terms a person looks very much like an employee, yet there is a desire to treat them as a contractor.

(b) Often, it is the employer may want to avoid an employment relationship for a variety of reasons, such as to (for example) escape having to pay superannuation contributions or workers compensation premiums, provide paid leave, comply with award provisions as to wage or working hours, risk of unfair dismissal claims etc.

(c) However, drafting a contract specifically to disguise an employment relationship as an independent contracting arrangement may evoke the sham contracting provisions of the FW Act.

(d) The FW Act prohibits employers from:

(i) misrepresenting an employment relationship or a proposed employment arrangement as an independent contracting arrangement;

(ii) dismissing or threatening to dismiss an employee for the purpose of engaging them as an independent contractor; and / or

(iii) making a knowingly false statement to persuade or influence an employee to become an independent contractor.

(e) The FW Act prohibits sham arrangements and imposes fines for each breach of the provisions and workers may seek compensation from their employer for any loss suffered by them as a result of a breach of the provisions.

(f) In addition to potential claims for back pay and penalties from the ATO for non payment of tax and superannuation, sham contracting is unlawful under the FW Act with maximum penalties of up to $12,600 for an individual and $63,000 for a company.

4.3 Accessorial liability

(a) Under the FW Act the court may order a person to pay a pecuniary penalty if that person has contravened what is known as a civil remedy provision, which essentially means that someone can be penalised or fined by a court if they brake certain workplace laws.

(b) For advisors, it is critical to understand that under section 550 of the FW Act other persons may also be penalised or fined where they themselves are '*involved in a contravention of a civil remedy provision'*.

(c) Accessorial liability occurs when a person or company is involved in the contravention of a workplace law. When this happens, they are treated the same way as the employer responsible for the contravention. They can be ordered by a court to pay employees' unpaid wages and entitlements, as well as penalties for their involvement in the contravention

(d) A person is *involved in* a contravention of a civil remedy provision if, and only if, the person has:

(i) assisted, recommended or caused the contravention; or

(ii) influenced the contravention (eg. by making threats or promises); or

(iii) was concerned in or was a party to the contravention; or

(iv) conspired with others, which resulted in the contravention.

(e) It is essential that 'actual knowledge' is possessed by the person about the contravention, which may be inferred from '*a combination of suspicious circumstances and a failure to make an inquiry*'[10].

(f) However, mere knowledge of the contravention alone is insufficient to be tied to the conduct, and there must be some sort of 'practical connection', whereby the person is 'involved in' the conduct by some conduct which 'implicates' them in the offending conduct.

(g) As it currently stands, the elements of the law of accessorial liability are somewhat unsettled. However, the Fair Work Ombudsman (**FWO**) has recently expressed a willingness to use the laws to pursue external business advisors who facilitate the exploitation of workers.

(h) A particularly noteworthy case of this occurred in 2018[11] when the FWO secured a penalty of over $50,000 against a firm of accountants called EZY Accounting 123 Pty Ltd (**EZY**) that provided payroll services to an employer who was found to have been systemically underpaying its workers.

(i) Despite EZY's arguments of only following the instructions of the employer, it was found by the court that EZY had been involved in contraventions of the FW Act because it had actual knowledge of the underpayments from a previous audit and did nothing to rectify those pay rates.

(j) In order to reduce the risk of being captured by the accessorial liability provisions of the FW Act, we recommend that advisors:

(i) familiarise themselves of the obligations under the FW Act and other workplace laws and understand the limits of their knowledge. Ignorance of the law is not a defence;

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[10] *Compaq Computer Australia Pty Ltd v Merry* (1998) 157 ALR 1 at 5 per Finkelstein J

[11] *EZY Accounting 123 Pty Ltd v Fair Work Ombudsman* [2018] FCAFC 134

(ii) do not give advice on issues that are not completely understood;

(iii) do not turn a blind eye and make enquiries to confirm compliance with relevant workplace laws; and

(iv) if they become aware of potential contraventions, consider seeking advice from an appropriate external advisor.

Clifford Gouldson Lawyers

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