



Leanne Tully
Senior Lawyer
Workplace Relations

Leanne has experience in advising clients on all aspects of employment law. Leanne has advised both businesses and individuals on:

- employment issues such as employment contracts,
- employee entitlements,
- termination,
- unfair dismissals,
- sexual harassment and discrimination,
- WorkCover and
- employment policies and procedures.

Leanne also has experience in acting for people who are seriously injured at work.

Independent Contractors under the Spotlight

When is a contractor not a contractor?

In a 'sham contracting' case decided on 5 April 2011, the Federal Court ruled that Risetop Construction Pty Ltd and its directors misrepresented that employment contracts were independent contractor agreements. Penalties were imposed on the company (\$10,000) and on two directors (\$2,000 each).

Sham contracting is under renewed scrutiny from several bodies, including:

- the Australian Building and Construction Commissioner ('ABCC'), which is conducting an Inquiry;
- the CFMEU, which is pursuing a campaign for tougher laws in this area;
- the Australian Taxation Office, which has a stated focus on sham contracting.

In this edition of *Employment Alert* we will review the sham contracting provisions of the *Fair Work Act 2009* ('FW Act') and discuss the implications of determining whether arrangements with a worker lead to an employment relationship or not.

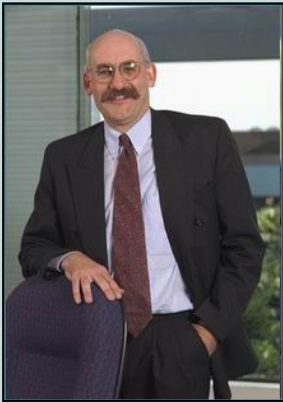
What is 'sham' contracting?

Sometimes an employment relationship exists, even though the paperwork indicates a relationship of principal and independent contractor (a contract for services). This can result from confusion or mistake, due to the difficulty of identifying the appropriate label for the relationship.

In some cases, the wrong label is applied deliberately or recklessly by the employer/principal or the employer/principal attempts to cut costs by converting employees into independent contractors. This latter type of behaviour is the target of the FW Act sham contracting provisions, which may be summarised as follows:

1. An employer (or prospective employer) must not misrepresent that a contract of employment is a contract for services under which the individual performs (or would perform) work as an independent contractor. The employer has a complete defence if it proves it did not know and was not reckless as to whether the contract was for employment or for services.

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Peter Andrew
Special Counsel
Workplace Relations

Peter has extensive experience in workplace relations issues, including unfair dismissal litigation, employment litigation and occupational health and safety issues.

Peter advises on issues including

- negotiation of executive terminations;
- drafting of employment and contractor agreements;
- leave entitlements;
- impact of workplace relations laws on business;
- termination and redundancy;
- workplace procedures including drafting of policies;
- transfer of business, particularly in relation to sale of business;
- restraint of trade;
- protection of intellectual property and other confidential information;
- employee discipline and performance evaluation.

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2. An employer must not dismiss, or threaten to dismiss, an employee in order to engage the individual to perform the same, or substantially the same, work under a contract for services.
3. An employer must not make a statement that the employer knows is false, in order to persuade or influence an employee (or former employee) to enter into a contract for services (for the same or substantially the same work).

These prohibitions are similar to the provisions operating under the *Workplace Relations Act 1996* ('WR Act') since June 2007. Although there have been only a handful of sham contracting cases, including two successful prosecutions brought by the Fair Work Ombudsman, the Courts appear likely to see an increase in the number of such cases in the construction industry, after a change in approach by the ABCC since Leigh Johns took over the reins in October 2010.

Misrepresenting the nature of the contract

In one case brought by the Fair Work Ombudsman, Centennial Financial Services Pty Ltd was found to have breached two of the sham contracting provisions in the WR Act – those relating to misrepresentation and dismissal.

The Court found that Centennial had misrepresented the nature of a new 'sales consultant agreement' presented to employees. Although the agreement purported to engage the sales consultants as independent contractors, they remained in an employment relationship with Centennial. In reaching this conclusion, the Court considered many factors, including the fact that Centennial retained ownership of any clients they introduced, expected that they work exclusively for Centennial, required them to attend the office at particular times, and required them to wear uniforms and carry Centennial business cards.

In another case, brought by the CFMEU against Nubrick Pty Ltd, the Federal Magistrates' Court found that the contracts were, in substance, contracts of employment and that Nubrick had misrepresented the nature of the contracts. However, Nubrick was not liable because it was able to prove that, at the time the representations were made, it did not know and was not reckless as to whether the contracts were contracts of employment.

Dismissal in order to re-engage as contractors

An employer may be in breach of the provisions relating to dismissal of an employee, even if there is no explicit termination of employment; for example, where there is a 'constructive dismissal' because the employer behaves in such a way that the employee is entitled to treat the employment as at an end.

In the Centennial case, the Court found that Centennial had dismissed the employees in order to engage them to perform the same duties under the new agreement, on a 'commission only' basis, instead of on a salary basis. The dismissal was not explicit, but resulted from the way the company presented the new agreement, showing an intention not to be bound by the existing employment relationship.

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Frances Anderson
Senior Lawyer
Workplace Relations

Frances has considerable experience in workplace relations, having practiced exclusively in this area since 1989, both in Australia and overseas. She has advised employers across several industries and business sectors in both industrial relations and employment law.

Frances has given comprehensive advice in relation to a broad range of workplace relations issues in Australia, including employment related litigation; discrimination complaints; enterprise bargaining; employment contracts; and workplace policies.

Frances has also advised on the employment related implications of sale of business/sale of shares transactions.

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Managers can be liable

In the Centennial case, the director and the HR manager were found to have breached the WR Act. The HR Manager defended the claim relating to misrepresentation of the nature of the new agreement, by arguing that he did not know and was not reckless as to the true nature of the contract. However, the Court held that only the employer company could rely on such a defence. (In this case, the company did not establish that defence as the director did not give evidence, and the HR Manager was not in a position to give evidence on the company's state of knowledge).

Even though the HR Manager was acting under the director's instructions, and apparently had little control over the situation, the Court found that the HR Manager was "knowingly concerned" in Centennial's contravention of the legislation and therefore liable as an accessory.

Grey area between employment and contracting

For many companies, the issue of whether a worker is an employee or an independent contractor is not clear cut. Even if a company is not "reckless", and does not otherwise breach the FW Act sham contracting provisions, it may still find that it faces unexpected liabilities in the form of unfair dismissal claims and claims for employment entitlements, if it inadvertently mis-labels a relationship as one of independent contracting. Courts can look behind the formal contract to determine the true relationship between the parties.

For example, in the case of *Williams v JMZ Roof Restorations*, Fair Work Australia held that a painter who was engaged as a contractor using an ABN, was in fact an employee, and was therefore entitled to bring an unfair dismissal claim. FWA noted that Williams was an "integral part of the business" of JMZ and was "not conducting his own business during the time he was engaged" by JMZ.

The "absence of a simple and clear definition which explains the distinction between an employee and an independent contractor" was noted by Justice Bromberg in a Federal Court case decided on 13 April 2011. His Honour stated, "Workers and those who employ or engage them require more clarity from the law. This is particularly so when important legislation such as the Fair Work Act...steadfastly avoided defining what is an employee, yet demand (on pain of civil penalty) that there be no misrepresentation as to the nature of the work relationship".

While defining the term "employee" has been too difficult for the parliament, it is a task that businesses are required to undertake on a regular basis.

The decision - to employ or to contract?

Contracting remains a popular option for both 'employer'/principals and workers. For principals, contracting offers flexibility, efficiency, reduced risks and the ability to limit Union influence in the workplace. For some workers, it means greater flexibility, independence and profitability.

However, from the perspective of Unions and some workers, contracting can represent a potential threat to workers' rights to minimum wages, conditions, leave entitlements, superannuation and job security. Contracting can also be seen as a risk to the tax base resulting from contractors' ability to split income and claim deductions, and from failure to report personal services income.

Independent contracting arrangements may come under scrutiny through sham contracting prosecutions, but also through tax office investigations, and claims by workers for employment entitlements.

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Companies should carefully consider the true nature of the arrangements they are proposing to make with workers, remembering that it is not sufficient simply to call a relationship 'independent contracting' if it does not meet the necessary requirements.

Companies should also be careful not to pressure employees into becoming independent contractors. Even if workers initially agree to the new terms of engagement, they may take a closer look at their legal rights if they find that they are worse off than they were as employees. This may lead to investigation and prosecution some time down the track.

Implications for business owners

When engaging workers as employees or independent contractors, business owners should:

- Seek advice or familiarise themselves with the legal tests for determining whether a person is an employee or independent contractor;
- Choose whether to offer an employment or contracting arrangement, taking into account the legal tests;
- Check obligations to pay WorkCover, superannuation and payroll tax;
- Ensure terms and conditions of engagement are agreed to in writing and signed by both parties.

For advice on independent contracting, including whether an employment contract or contract for services is appropriate for a particular role, contact the Workplace Relations Team at Moores Legal on 9898 0000.

Leanne Tully, Senior Lawyer
Benson Siong, Trainee

The Moores Legal Workplace Relations team

For further advice and guidance on any employment issue and how it may impact your business and commercial operations, contact the Workplace Relations team at Moores Legal.

Moores Legal is a law firm servicing companies and businesses, Not for Profit organisations and individuals across Melbourne in the areas of Commercial Law, Workplace Relations, Property Law, Not for Profit Law, Aged Care, Elder Law, Estate Planning, Superannuation & Structuring, Dispute Resolution, Family Law and Personal Injury Law.

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