

Do you Employ or Contract - That is the question being asked by the ATO right now.

Many small businesses are now being asked by the ATO whether they engage staff as contractors or as employees.

The distinction is one of some considerable importance for several reasons, the most significant being:

- Taxation obligations, including payroll tax and PAYG
- Workers compensation payments
- Applicability of any relevant award rates of pay
- Leave and other statutory benefits or entitlements
- Ownership of intellectual property created/discovered in the course of engagement
- Application of unfair dismissal laws and remedies
- Superannuation payments
- Insurances and risk
- Compliance with statutory obligations

The incorrect form or method of engagement can have serious and costly consequences for one or both parties.

Further, the Fair Work Act prohibits 'sham contracting arrangements'. This is where an employer treats a worker as an independent contractor in an attempt to avoid meeting employee entitlements. The employer who converts staff to contractors is acting illegally, and may well face stiff penalties for avoiding workers compensation laws for example, as well as prosecution for tax evasion and flaunting compulsory superannuation law.

Unfortunately, there is no single, objective and universally accepted test that can be applied to quickly and conclusively determine whether a person is an employee or an independent contractor. Australian Courts and tribunals, together with government bodies such as the ATO, have all emphasised that each case must be considered on its merits and requires a detailed assessment of the terms of engagement and the facts of the actual working relationship.

Whether a worker is an employee or a contractor is determined by the nature of the arrangement, not by the label used to describe the relationship.

1. The Control Test

The control test determines the nature of the relationship between a person who engages another to perform work and the person so engaged by assessing the degree of control which the former can exercise over the latter.

- a) **Employees** are not only told what work to do, but also how, when, and where it is to be carried out.
- b) **Contractors** are able to provide a service or deliver a certain product at their own discretion and are able to delegate tasks to others.

2. Organisation/Integration Test

- a) **Employees** generally only work for one employer and are an integral part of the employer's ongoing business, on an ongoing basis.
- b) **Contractors** are free to offer services to many and will work for many to mitigate business risk. Contractors are contracted for a specific project.

3. Contract for a Result: If a contract is to achieve a specific result, there is a strong indication that it is a contract FOR service and therefore a relationship of **principal/contractor**.

4. Delegation: If the worker is contractually obligated to perform the work and is unable to delegate or subcontract, this would reflect a relationship of **employer/employee**.

5. **Risk:** Where the worker bears little or no risk of the cost arising out of an injury or defect in the work, this would reflect a relationship of **employer/employee**.

6. **Tools and Expenses:** If the worker is required to supply their own tools and equipment and to pay for their own expenses and other overheads, this would reflect a relationship of **principal/contractor**.

7. **Basis of Contract:** If the worker provides services through a corporate entity or trust, this would reflect a relationship of **principal/contractor**.

8. **GST:** If a worker is paid as a result of submitting invoices, which include GST, this would reflect a relationship of **principal/contractor**.

9. Other indicia indicating a relationship of employer/employee:

- a) Circumstances surrounding the formation of the contract;
- b) The right to suspend or dismiss the person engaged;
- c) Provision of benefits, such as annual leave, sick leave, long service leave; and/or
- d) The requirement that the worker wear a company uniform.

Getting it Right

- Consider the reality of the relationship;
- Make sure that, operationally, you follow the rules;
- Ensure you have written contracts and documentation that reflects the reality of the relationship; and
- Act consistently with the terms of any contract.

The Australian Taxation Office is currently carrying out audits on several small and medium businesses, focusing on some specific industries and has maintained its focus on those businesses that engage contractors. The ATO, as well as the Fair Work Ombudsman, Fair Work Australia and WorkCover Queensland, are interested in investigating whether or not the contractor/principal relationship is a genuine one or if it is in fact a relationship of employee/employer and would therefore be deemed a sham contracting arrangement. It is imperative to ensure that if you are engaging contractors, you have the appropriate documentation in place and are carrying out your business in accordance with the requirements placed on a principal/contractor relationship. There are substantial penalties for getting this wrong and as such this is an opportune time to contact **Michael Sing Lawyers Pty Ltd** to seek advice in respect of your business activities and to ensure that your business is fully protected from any investigation carried out by the above organisations. For advice on reviewing or updating your current contractor or employment agreements, please contact our Gold Coast team on (07) 5597 8888 or our Brisbane team on (07) 3229 6099.



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