5

Commercial arrangements

5.1 Some have described independent contracting as a commercial relationship, while others consider it requires industrial or workplace relations regulation. This chapter discusses the operation of deeming provisions where independent contractors have their status altered, to be protected by industrial regulation, as an employee. Further examination of the trade practices and unfair contracts legislation is included to determine the extent of applicability to independent contractors. Avenues of redress where unconscionable conduct is present are also discussed.

5.2 Business structures are then discussed to identify the form and incidence of possible sham arrangements or disguised employment. Possible drivers for employers to enter into different working arrangements and pressures for independent contractors to incorporate are reviewed. A summary of tax minimisation strategies is also included.

Deeming

5.3 Independent contracting and labour hire arrangements have presented challenges for legislators to determine the most appropriate method to protect workers where in situations of unequal bargaining power. Discussion of this legislation is warranted as a context to consider strategies to ensure consistency of protection for workers across Australia.

5.4 Denying the presence of an employment relationship through the use of contracts or other business arrangements were concerns reported to the Committee. Rigid definitions and the ability to circumvent legislative intent through contractual arrangements have prompted legislatures to consider other options. These concerns have prompted some state governments to introduce 'deeming' legislation to ensure protections for certain workers.

5.5 Deeming involves the power to declare persons who work under a contract for service, such as independent contractors, to be employees. Deeming provisions are different from common law tests because they are designed to classify as employees groups of workers with service contracts. Common law tests can only be applied to individuals on a case-by-case basis.[1]

5.6 Queensland and NSW have been the more prominent advocates in introducing deeming legislation. South Australia considered further deeming amendments with the South Australian *Industrial Law Reform (Fair Work Bill)* 2004 but these were not supported by the Legislative Council, and hence were not included in the final Act.[2] Tasmania is currently considering provisions similar to Queensland as announced in a discussion paper released last year.[3]

5.7 In some states, for example Tasmania and Western Australia there is no specific workplace relations deeming legislation. However, there is legislation which pertains to industrial relations and which effectively deems by expanding the definition of employee to include for example outworkers, contract cleaners, labour hire workers and piece workers.[4] Discussion of other labour legislation which has broader coverage is included later in the chapter.

5.8 The WR Act has no deeming provisions, and therefore this applies to Victoria, ACT and the Northern Territory. In Victoria there is improved protection of clothing industry contract outworkers, and specific provision for minors with the *Child Employment Act 2003*.[5]

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1 ACCI, *Submission No. 25,* pp. 19-20; NSW Government, *Submission No. 35*, p. 35.

2 South Australian Attorney General's Department, Update of 2004 Index of South Australian Legislation, Industrial Law Reform (Fair Work) Act 2005, p. 9, accessed 11 March 2005, <www.parliament.sa.gov.au/leg/index/update.pdf>; Workplace express, 10 March 2005, Finally, SA's new IR bill gets through Parliament, accessed 11 March 2005, <www.workplaceexpress.com.au/news_print.php?selkey+24248>.

3 DEWR, *Exhibit No. 25*, p. 18.

4 DEWR, *Exhibit No. 25*, p. 18.

5 Vic. Government, *Submission No. 71*, pp. 6-7; DEWR, *Exhibit No. 25*, pp. 18-19.

Queensland

5.9 The Queensland Government states that:

> The increasing move away from the conventional employee/employer relationship towards workers engaged under labour hire arrangements and under dependent contractor status, has effectively taken these workers outside of the industrial relations system and the benefits and protections associated with being defined as an employee under relevant industrial laws.[6]

5.10 Section 275 of the Queensland *Industrial Relations Act 1999* (Qld IR Act) gives the Queensland Industrial Relations Commission (QIRC) the power to declare persons who work under a contract for services to be employees (employee 'deeming').[7]

5.11 Persons or workers that this deeming applies to includes: outworkers, lessees of equipment or vehicles, drivers wholly or partly owning their vehicles and persons working as partners in a business or association. The list of criteria that Section 275 of the Qld IR Act allows the Commission to declare a class of contractors to be employees includes:

- the relative bargaining power of the class of persons; or
- the economic dependency of the class of persons on the contract; or
- the particular circumstances and needs of low-paid employees; or
- whether the contract is designed to, or does, avoid the provisions of an industrial agreement; or
- whether the contract is designed to, or does exclude the operation of the Queensland minimum wage; or
- the particular circumstances and need of employees including women, persons from a non-English speaking background, young persons and outworkers.[8]

5.12 Section 275 has not been widely used. Examples of cases relating to independent contractors were provided to the Committee. One application to the QIRC was dismissed with shearers being found to be contractors rather then employees (*AWU v Hammonds Pty Ltd*). Another case considered that security workers previously being engaged as employees should continue to be considered as employees

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6 Qld Government, *Submission No. 66*, pp. 6-7.

7 Qld Government, *Submission No. 66*, p. 7.

8 DEWR, *Exhibit No. 25*, p. 17; ASU, *Submission No. 53*, p. 9.

rather than as independent contractors (*ALHMWU v Bark Australia Pty Ltd*).[9]

New South Wales

5.13 Schedule 1 of the NSW *Industrial Relations Act 1996* (NSW IR Act) deems certain types of workers to be employees. The NSW Government states that the deeming provisions recognise that a number of categories of workers exist who are often in weak negotiation positions. In many instances, the relationship which exists is not substantively different to that of employee and employer, and hence should be covered by the protection of generally accepted standards of industrial regulation.[10]

5.14 The NSW legislation includes:

- a range of specific occupations, such as cleaners, carpenters, joiners or bricklayers, plumbers, drainers or plasterers, painters and clothing outworkers;
- power to deem others to be employees by regulation,
- a system of contract determination, and
- a process to test if employment contracts are unfair.[11]

5.15 The NSW Government considers that if there were not deeming provisions, there may be a significant degree of inequality in bargaining power between the worker and the provider of work.[12]

Advantages and disadvantages of deeming

5.16 Supporters of deeming provisions generally point to the need to protect workers from unequal bargaining power to negotiate reasonable contract conditions. Submissions of support were mainly received from state governments and unions.[13] The advocates of deeming highlight that this approach 'overcomes some of the shortcomings of a rigid definition' and case law to identify who is an employee.[14]

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9 Qld Government, *Submission No. 66*, p. 7; NFF, *Submission No. 39*, p. 8; AWU v Hammonds Pty Ltd [1999] (B885 of 1999) QIRC, 15 November 2000; ALHMWU v Bark Australia [2001] QIRC 22, 28 February 2001; 166 QGIG 254.

10 NSW Government, *Submission No. 35*, p. 35.

11 NSW Government, *Submission No. 35*, p. 35; Qld Government, *Submission No. 66*, p. 8.

12 NSW Government, *Submission No. 35*, p. 35.

13 Vic. Government, *Submission No. 71*, p. 7; NSW Government, *Submission No. 35*, p. 35; Qld Government, *Submission No. 66*, p. 41; ASU, *Submission No. 53*, p. 9; CFMEU, *Submission No. 5*, Appendix 13: ACTU Submission to NSW Labour Hire Task Force, pp. 15-16; see also Australian Lawyers Alliance, *Submission No. 55*, pp. 3, 14.

14 Qld Government, *Submission No. 66*, p. 41; Prof. A. Stewart, *Submission No. 69*, p. 6-7.

5.17 In contrast, detractors of deeming approaches included employer organisations, independent contracting bodies and some in the law profession. Critics cite the piecemeal approach, disregard of the common law distinction, and the lack of consideration of the substantive nature of working relationships as being of considerable concern.[15]

Supporters

5.18 The NSW Government states that deeming affirms the role of government in protecting persons who enter into contracting arrangements with limited information or misunderstanding of how the relationship will operate. It achieves this goal by a variety of means, including:

- both general and specially tailored legislative provisions, including the definition of 'employee';
- expanding the category of employee by deeming certain classes of 'at risk' workers to also be employees; and
- providing remedies for workers in unfair or exploitative relationships.[16]

5.19 The NSW Government acknowledges that workers identified by deeming provisions would otherwise be considered to be independent contractors under common law. They are viewed by both the courts and legislature to be 'in business for themselves'. They state that, like employees, there may be a significant degree of inequality in bargaining power between the worker and the provider of work.[17]

5.20 The NSW Government rejects that the Commonwealth should move to nullify the effect of the NSW deeming provisions.[18] Further discussion of this issue is raised in Chapter 6 under pursuing consistency in independent contracting.

5.21 Other supporters indicate that deeming provisions provide lower paid workers protection from exploitation in unfair contracts. It was stated that the idea that employees have the right to negotiate conditions of work that suit their individual needs does not reflect the reality and the majority of outcomes. The costs, length of the process

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15 HIA, *Submission No. 61*, p. 1; ACCI, *Submission No. 25*, p. 6; Ai Group, *Submission No. 49*, pp. 24-25; MBA, *Submission No. 22*, p. 14; NFF, *Submission No. 39*, p. 7; ICA, *Submission No. 20*, p. 8; AICA, *Submission No. 64*, p. 12; Prof. A. Stewart, *Submission No. 69*, pp. 7-8; Mr. T Hulett, Law Council of Australia, *Transcript of Evidence*, 27 April 2005, p. 62.

16 NSW Government, *Submission No. 35*, p. 5.

17 NSW Government, *Submission No. 35*, p. 35.

18 NSW Government, *Submission No. 35*, p. 36.

and the uncertainty are major disincentives to take action to seek redress.[19]

5.22 Australian Lawyers Alliance highlighted that the use of deeming legislation would be of benefit to ensure that all workers, regardless of their nominal employer, are covered by the relevant workers' compensation scheme.[20]

5.23 The CFMEU supports the extension of the definition of the employer to include partnerships, group training schemes and labour hire agencies.[21] The Australian Services Union stated that the use of deeming provisions to treat dependent contractors such as family day care workers as employees for the purpose of wages and conditions and unfair termination of contract should be considered.[22] The ACTU provide some support for deeming; however, seek greater definitional clarity that truly reflects the working relationship.[23]

Detractors

5.24 DEWR states that inappropriate and unduly complex state legislation restricts independent contractors' ability to maximise their productivity and contributions to the Australian labour market. Further, deeming also inhibits businesses' ability to manage their workforce so that it can be augmented or restricted depending on work demands.[24]

5.25 Ai Group comments that

> …despite the fact that an individual may, under common law, legitimately be an independent contractor, Federal and state governments have enacted legislation which deems certain independent contractors to be employees for particular purposes.[25]

5.26 They also cited concern with the disparate nature of the types of workers deemed to be employees in Schedule 1 of the NSW IR Act, and the potential for lobbying to increase the range of workers included.[26]

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19 Qld Government, *Submission No. 66*, p. 35; Mr M. Anderson, *Submission No. 70*, p. 4.

20 Australian Lawyers Alliance, *Submission No. 55*, p. 3.

21 CFMEU, *Submission No. 5*, Appendix 13: ACTU Submission to NSW Labour Hire Task Force, p. 16.

22 ASU, *Submission No. 53*, pp. 9, 12.

23 ACTU, *Submission No. 60*, pp. 18-20.

24 DEWR, *Exhibit No. 25*, p. 21.

25 Ai Group, *Submission No. 49*, p. 25.

26 Ai Group, *Submission No. 49*, pp. 24-25.

5.27 The Ai Group comment that some statutory provisions concerning independent contractors are appropriate.[27]

5.28 In South Australia, the *Industrial and Employee Relations Act 1994* includes examples that highlight the difficulty of distinguishing between employees and independent contractors. When a person packs goods under a contract for services at home they are deemed to be an employee, but not if they do so at a business's premises.[28]

5.29 SBDC also highlighted concern with the intent of South Australian legislation that has a broad definition of 'outworker' rather than restricting the legislation to the clothing industry, such as has occurred in other states. This would have implications for a wide range of professionals that work from home such as accountants, IT workers and sales persons.[29]

5.30 It was reported to the Committee that the ambiguity of independent contractor status creates commercial uncertainty, complexity and additional costs which lead to competitive handicaps for contractors.[30]

5.31 ACCI states that the confusion created by unfair contracts legislation and deeming extends beyond contracts for services with individuals. It also impacts on other commercial relationships between franchisers franchisees, contractors and sub-contractors.

5.32 ACCI supports:

- removing deeming of individual contractors as employees from the Australian system of labour law;
- precluding the operation of state deeming provisions;
- ending applications to state authorities under state deeming provisions;
- reversing any previous declarations deeming contractors or classes of contractors to be employees; and
- retaining the protection of clothing industry outworkers, and only including such regulation in other industries in exceptional circumstances.[31]

5.33 The Committee considers that strategies to address the unequal bargaining power would be more effective at the source rather than

27 Ai Group, *Submission No. 49*, p. 24.

28 DEWR, *Exhibit No. 25*, p. 21.

29 SBDC, *Submission No. 58*, p. 5.

30 HIA, *Submission No. 61*, p. 1; Courier and Taxi Truck Association, *Submission No. 50*, p. 6.

31 ACCI, *Submission No. 25*, pp. 28-29.

overlaying a blanket solution which does not respect common law or contractual arrangements.

5.34 The Committee's view is that a lower cost, user friendly process for making determinations about employee or independent contractor status needs to be introduced with national coverage. In addition a contract review process needs to be retained to challenge unfair contracts. The adoption of the method to determine status, as proposed in the previous chapter, would assist in this process. The issues are considered further later in this and the next chapter.

Other legislation

5.35 Other regulatory areas of law have a broader scope than the common law distinction between independent contractors and employees. Similar to the debate about the advantages and disadvantages of deeming in industrial or workplace relations matters, there is dispute about the necessity of such broad coverage. Areas of consideration include:

- occupational health and safety legislation imposing duties beyond the traditional concept of the employment relationship;
- workers' compensation legislation applying to certain workers under a contract for service;
- payroll tax covering contractors performing work other than pursuant to a trade or business which they carry on and do not sub-contract to anyone else;
- discrimination legislation applying to both contractors and employees;
- long service leave in some jurisdictions; and
- the superannuation guarantee which provides that if a person works under a contract that is wholly or principally (more than half) for the labour of the person, the person is an employee of the other party to the contract.[32]

5.36 In the field of OHS legislation, critics of the deeming approach state that:

> The deemed inclusion of a diverse range of workers, represents a potpourri of examples without any single defining principle, apart from some inchoate notion that they represent socially desirable areas of coverage.[33]

32 Qld Government, *Submission No. 66*, p. 7; and Ai Group, *Submission No. 49*, p. 25.

33 MBA, *Submission No. 22*, p. 16 citing Clayton A, Johnstone R and Sceates S, 2003, *The Legal Concept of Work-Related Injury and Disease in Australian OH&S and Workers' Compensation*

5.37 Workers' compensation arrangements were frequently mentioned as causing particular concern with deeming provisions. The Insurance Council of Australia supports a clearer definition, and is cautious on the deeming approach.[34]

5.38 Workers' compensation coverage is required if independent contractors work through an agency, yet income protection insurance would normally be sought when they are not working through an agency.[35] HIA outlined their concern with state systems which bring independent contractors into the industrial relations systems. Additionally OHS regulation adds to the cost of using contractors, as does payroll tax, workers' compensation and superannuation.[36] This issue of costs is discussed in more detail in a later section on Business structures.

5.39 DEWR states that OHS and discrimination laws:

> … are not 'deeming' provisions which change the nature of the common law relationship between the hirer and worker. Rather, these laws often use the term 'employment' as a definitional device to describe the classes of people to be covered for that legislative purpose. The breadth of the definition will depend on the policy objective of the legislation [in] question. For example, OHS and discrimination laws have generally been drafted to apply to workers generally, irrespective of whether they are hired as employees or independent contractors. This is because the purpose of these laws is to seek to protect people in their working lives generally and this may be the reason they are framed broadly.[37]

5.40 The Victorian and Queensland governments question quarantining workplace relations legislation in this way, suggesting that if there is a good policy objective to do so then there is justification. They cite the Australian Government introducing the PSI legislation to clarify

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Systems, ANU National Research Centre for OHS Regulation; Australian Lawyers Alliance, *Exhibit No. 24:* National Research Centre for OH&S Regulation: Working Paper No. 3. *The legal concept of work-related injury and disease in Australian OH&S and Workers' Compensation Systems*, April 2002, p. 19.

34 Insurance Council of Australia, *Submission No. 11*, p. 3.

35 AICA, *Submission No. 64*, p. 15.

36 HIA, *Submission No. 61*, p. 1.

37 DEWR, *Exhibit No. 25*, p. 19.

independent contractor status in relation to taxation to reduce revenue moving out of the PAYG system.[38]

Deeming as a consistent approach

5.41 There are a range of views on the need for providing some protections to workers, and the use of deeming to encompass independent contractors and labour hire workers within the industrial relations systems.

5.42 However, the piecemeal approach and different coverage in various jurisdictions suggests that there is no consistent adoption of deeming. In addition, some legal practitioners had reservations on the creation of an artificial construct to override in some cases the existence of a commercial relationship. This supports business organisations' other criticisms of deeming.

5.43 Professor Stewart states that deeming is usually a reactive strategy, relying on identifying a group or occupation of workers and invoking the relevant deeming mechanism.[39] Additionally, deeming provisions are generally directed at the status of a class of workers and do not address the reality that an individual worker can operate in a legitimately independent way as a business. That is, the worker is considered an employee regardless of their preference or actual circumstances.[40]

5.44 Alternatives suggested by submissions include:

- a registration system of contractors which would negate the need for deeming legislation.[41]
- a consistent appropriate definition of 'employment' or 'employee' depending on the legislation involved and the policy goal across jurisdictions.[42]

Power of relationships

5.45 The states' approach to resolve the imbalance of bargaining also relates to recent cases where it has been argued that employees have been requested to consider independent contracting (some would say with coercion), and new recruits are required to be engaged as

38 Qld Government, *Submission No. 66*, p. 7; Vic. Government, *Submission No. 71*, p. 20.

39 Prof. A. Stewart, *Submission No. 69*, pp. 7-8.

40 ACCI, *Submission No. 25*, pp. 19-20; AICA, *Submission No. 64*, p. 12.

41 MBA, *Submission No. 22*, p. 15.

42 Prof. A. Stewart, *Submission No. 69*, p. 9.

independent contractors.[43] One description of this change in arrangements suggests that:

> The nature of the work, the payer of remuneration and the workplace itself does not change. This type of arrangement can be termed as 'the Friday employee becomes the Monday independent contractor.
>
> The arrangement, although agreed to by both the individual and the principal, is generally speaking, an attempt to free the employer from a range of costs and obligations eg workers' compensation and superannuation costs.[44]

5.46 Therefore, methods to determine the appropriate working relationship status are required. It has been suggested that access to the Federal Magistrates Court would assist in providing a simpler and more accessible alternative to litigation in the federal arena. It was stated the costs of current court action are prohibitive.[45]

5.47 Other suggestions include use of the Australian Industrial Relations Commission (AIRC) as an arbitral body to issue a certificate then apply to the court if seeking a variation or appeal.[46] However, the Federal Magistrates Court was considered by some to be a more appropriate forum to consider possible commercial contracts than a specialist body (the AIRC) that specialises in contracts of employment.[47]

5.48 Independent contractors are not covered by industrial legislation, unless a court challenge is made to their particular status. Nor would deeming provisions be available unless so specified.

5.49 This raises avenues of redress and what should be possible or appropriate representation. Deeming overrides the existence of commercial relationships. Commercial relationships are regulated in part through the TPA. Therefore, consideration of this legislation and unfair contracts as applying to independent contractors is required.

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43 National Union of Workers, *Submission No. 47,* p. 13.

44 Courier and Taxi Truck Association, Submission No. 50, pp. 4-5; see also CFMEU, *Submission No. 5*, Appendix 6: CFMEU submission to Review of Business Taxation, 1999, following paragraph 4.5.

45 DEWR, *Exhibit No. 25*, p. 20; see also Mr A. Cameron, RCSA, *Transcript of Evidence*, 26 April 2005, p. 27.

46 Vic. Government, *Submission No. 71*, pp. 30-32.

47 Canberra Business Council, *Submission No. 30*, p. 3; Labour Force Australia, *Submission No. 26*, p. 4.

Trade Practices Act 1974

Commercial relationships

5.50 It was stated that independent contractors are seen as individuals who organise their work through a commercial contract, rather than through an employment contract. This view is recognised by many of the submissions to the inquiry.[48]

5.51 ACCI in their submission state that commercial relationships are often ones of substantial dependence and considerable variation in economic size between the principal and the contractor.[49]

5.52 In addition, ICA argue that independent contractors are 'businesses in their own right.'[50] It is the WR Act that regulates the employment relationship. Therefore, as the common law definition of employee excludes independent contractors, the TPA being a commercial regulation, could be considered a more appropriate framework for independent contracting relationships. ICA state that:

> The regulation of labour under the Trade Practices Act is an important tool which releases people from being treated as a commodity.[51]

Trade Practices Act: background

5.53 The object of the TPA is to enhance the welfare of Australians through the promotion of competition and fair trading and to offer consumer protection. The TPA provides guidelines for the protection of anti-competitive behaviour, often described as monopolistic business practices, and acts as a guiding principal as to how companies conduct business.[52]

5.54 The laws regulating competition, contained in Part IV of the TPA, are comprehensive and extensive. Practices such as collusive agreements (preventing contractors from getting together in order to maximise their negotiating power), exclusive dealings, price discrimination, and the misuse of market power to eliminate or damage a competitor, false representation and misleading advertising are deemed illegal and thus prohibited; however specific exemptions from the TPA are

48 For example ACTU, *Submission No. 60*, p. 11; ICA, *Submission No. 20*, p. 5; DEWR, *Exhibit No. 25*. p. 5; NSW Government, *Submission No. 35*, p. 11.

49 ACCI, *Submission No. 25*, p. 23.

50 ICA, *Submission No. 20*, p. 5.

51 ICA, *Submission No. 20,* p. 15.

52 The *Trade Practices Act 1974* was Act No. 51 of 1974 as amended, its long title is: An Act relating to certain Trade Practices.

possible.[53] Such an exemption could be authorising a collective bargaining arrangement for a group of independent contractors.[54]

5.55 Issues associated with unfair contracts are contained in Part IV of the TPA which deals with restrictive trade practices. Section 45 deals with contracts, arrangements or understandings that restrict dealings or affect competition. Section 45(A) deals with contracts, arrangements or understandings in relation to prices. All of these have a bearing on, but are not limited to, unfair contracts.

5.56 ACCC is the regulatory body with the responsibility of enforcing trade practices law. Its key role is to attempt to educate, persuade or influence businesses into pursuing their interests within the legally defined boundaries of fair competition. The major emphasis of the ACCC is on anti-competitive business practices.

5.57 In recent times amendments to the TPA that are related to issues of this inquiry have been proposed. The main purpose of the TP Bill 2005 is to amend the TPA consistent with the government's response to the 'Review of the competition provisions of the Trade Practices Act 1974' (the Dawson Review).[55] Aspects of these amendments will be discussed later in this chapter.

5.58 If independent contractors are to wholly operate under commercial regulation then the effectiveness of the TPA for small businesses needs to be considered.

Collective bargaining

5.59 One mechanism for ensuring that small businesses and independent contractors do not suffer from inequality of bargaining power is through collective bargaining.

5.60 ACCC describe collective bargaining as:

> … an arrangement whereby multiple competitors in an industry come together, either directly or through the appointment of a representative to negotiate on their behalf, to negotiate the terms and conditions of supply with another, usually larger, business.[56]

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53 Specific exemptions may relate to authorisations, whereby the ACCC may grant an exemption on the basis of anti-competitiveness. ACCI, *Submission No. 25*, p. 43.

54 Treasury, *Submission No. 73*, p. 5.

55 *Review of the Competition Provisions of the Trade Practices Act*. (Also known as the Dawson Review), January 2005. Commonwealth of Australia; accessed 15 June 2005 <http://tpareview.treasury.gov.au/content/report.asp>.

56 ACCC, '*Authorising and notifying collective bargaining*', accessed 15 June 2005 <www.accc.gov.au/content/index.phtml/itemId/522935/fromItemId/314462>.

5.61 Under current legislation, ACCC can authorise collective bargaining arrangements that would otherwise risk breaching the TPA in circumstances where the public benefit of such an arrangement will overshadow the disadvantage caused by substantial lessening of competition.[57]

5.62 Difficulty in accessing authorisations was outlined by one group of independent contractors, the Australian Institute of Interpreters and Translators Inc (AIIT). The AIIT state the majority of their members do not have a choice between salaried employment and contracting. Furthermore, they are trapped into accepting contracting conditions over which they have no influence. To oppose the decline of their working conditions, contractors find themselves in 'jeopardy', under the TPA, by organising joint action or by trying to set minimum fees and conditions.[58]

> The interpreters find themselves isolated, outweighed, and powerless in their efforts to obtain acceptable conditions.[59]

5.63 A further example to illustrate the issue of reduced individual bargaining power can be found in the submission from the TWU, where it was made clear that owner-drivers generally suffer from an inequality of bargaining power with the companies they contract to.[60]

5.64 TWU state that the companies that owner-drivers negotiate with have extensive resources at their disposal to maximise their profits and minimise their liability to taxation, workers' compensation, superannuation and unfair dismissal in the negotiating process. Economic dependency becomes an issue for the owner-driver and a benefit for the contracting companies bargaining position.[61]

5.65 In reviewing authorisations for exemptions to the TPA to allow collective bargaining, the Treasury include in their submission, a list of authorisation determinations for the last ten years, from 1996 to 2005. The majority of the outcomes indicate that the determinations were granted or granted with conditions.[62] In this period of time, 136 matters were presented to the commission; 126 matters did not include trade union involvement.

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57 The Treasury, *Submission No. 73*, p. 5.

58 AIIT, *Submission No.* 37, p. 3.

59 AIIT, *Submission No*. 37, p. 3.

60 TWU, *Submission No*. 42, p. 3.

61 The TWU's involvement in seeking authorisations over the past ten years has not been extensive as they have made four representations. Further details can be found in: Treasury, *Submission No. 73*, Attachment No. 1, pp. 1-16.

62 Information sourced from the Treasury, *Submission No. 73*, Attachment No. 1, pp. 1-16.

5.66 In the ten year time frame there appeared to be no specific increase or decrease in union involvement, however there is an indication of a rise in collective bargaining. The increase in collective bargaining can not be directly correlated to unions in the bargaining process.[63]

Trade Practices Act Amendment Bill

5.67 Proposed amendments included in the Trade Practices Act Amendment Bill 2005 (TP Bill) are intended to reduce the regulatory burden on small businesses by implementing a process for collective bargaining by small business dealing with large business.[64] The Treasury state that the notification process will provide a streamlined and less costly alternative to the authorisation process.

5.68 One area of interest to the inquiry includes section 51(20(a)) of the TPA which allows trade unions to engage in collective bargaining regarding remuneration, conditions of employment, hours of work or working conditions of employees. The TP Bill 2005, if enacted, would exclude trade unions acting as agents for small businesses in collective bargaining negotiations.

5.69 Many submissions to the inquiry from employee groups maintain that independent bargaining power will be reduced through the introduction of amendments to the TPA, reducing union representation into the bargaining process. ACTU stated that

> … many independent contractors find themselves with little or no individual bargaining power when negotiating the terms of their engagement with their contractor or client.[65]

5.70 Concerns arise from the proposed reforms to the TPA, namely s93AB(9) of the TP Bill 2005. This is expressed by the TWU:

> In order [for] the TWU to negotiate collectively and within the legal limits set by Part IV of the Trade Practices Act 1974 (TPA) it is necessary for the TWU to obtain dispensation from these provisions of the TPA in the form of authorisations which may be granted by the ACCC.[66]

5.71 Section 93AB of the TP Bill 2005 states:

> (9) A notice given by a corporation under subsection (1) is not a valid collective bargaining notice if it is given, on behalf of the corporation, by:

63 Treasury, *Submission No. 73*, Attachment A.

64 Treasury, *Submission No. 73,* p. 5.

65 ACTU, *Submission No. 60,* p. 19.

66 TWU-Vic./Tas., *Submission No. 56,* p. 18.

a. a trade union; or

b. an officer of a trade union; or

c. a person acting on the direction of a trade union.[67]

Representation

5.72 Further evidence to the inquiry indicated that representation is an issue for independent contractors. The ACTU believe that independent contractors should have the rights and avenues for redress for representation.[68]

5.73 ACCI stated:

> If there is to be representation, whoever does it—whether it is unions, lawyers or whoever does contractor representation—it is a matter of recognising that that is a commercial relationship and that as a commercial relationship it does have some fundamentally different structures from direct employment.[69]

5.74 The NSW Office of Industrial Relations, in their submission to the inquiry, commented that there is no clear reason for excluding unions from being able to notify collective bargaining under the new scheme.[70] Furthermore, they state that the results under the scheme demonstrate how the TWU contributes to the achievement of 'settled and productive' relationships in the industry.

5.75 ICA suggested that the TPA may need to be amended to clarify that independent contractors come within the reach of the Act and unfair contracts are not excluded under the 'employment exclusion' provisions of the Act.[71]

Unfair contracts

5.76 As previously discussed in Chapter 2, an unfair contract is a contract that is harsh, unconscionable or is against the public interest.

5.77 Factors considered when deciding whether a contract is unfair are: the relative bargaining power of the parties, whether any undue influence

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67 Section 93AB (9), *Trade Practices Act Amendment Bill (No.1) 2005.* p. 51 accessed 15 June 2005; <http://parlinfoweb.parl.net/parlinfo/Repository/Legis/Bills/Linked/17020505.pdf>.

68 ACTU, Ms. N. Delavec, *Transcript of Evidence,* 26 April 2005, p. 42; Mr. P. Anderson, ACCI, *Transcript of Evidence,* 26 April 2005, p. 10.

69 Mr. P. Anderson, ACCI, *Transcript of Evidence,* 26 April 2005, p. 10.

70 NSW Government, *Submission No. 35,* p. 40.

71 DEWR-ICA, *Exhibit No. 69,* pp. 3 & 6-7.

or pressure or unfair tactics has been exerted, or whether the contract became unfair due to the conduct of the parties or variation to the contract.[72]

Federal and state legislation

5.78 Under Sections 127A-C of the WR Act, the Federal Court of Australia is empowered to examine contracts for services binding on an independent contractor which relate to performance of work. This section of the WR Act also provides a remedy for independent contractors.

5.79 The remedy is limited to an independent contractor who is a 'natural person'. However, there are constitutional limitations. It is also required that one of the parties be a Commonwealth authority, or a financial trading or foreign corporation, or relate to matters that take place in or are connected with a Territory.[73]

5.80 Amendments to the WR Act to remove its unfair contracts provisions in section 127A-127C were proposed, but not passed, in separate Bills in 1996 and 1999. DEWR stated that the removal of these provisions would be consistent with the Australian Government's policy that independent contracting arrangements should be regulated by commercial law, not workplace relations law.[74]

5.81 However there seems to have been a recent shift in approach with legislative changes associated with the building and construction industry. Additionally Freedom of Association provisions do not confine independent contractors to only be natural persons and therefore could include partnership arrangements or company structures.[75]

5.82 A brief summary of the unfair contracts legislation across the states is provided by DEWR:

- In NSW, the unfair contracts laws are found in Section 106 of the NSW IR Act. This allows the NSW Industrial Relations Commission to review 'any contract whereby a person performs work in any industry' which includes independent contractor arrangements;[76]

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72 *Trade Practices Act 1974*, Part IV, s. 45; *Workplace Relations Act 1996*, Division 3, Part VI, s. 127.

73 DEWR, *Exhibit No. 25*, p. 19. Natural persons do not include partnerships or companies.

74 DEWR, *Exhibit No. 25*, p. 20.

75 DEWR, *Exhibit No. 25*, p. 20; Vic. Government, *Submission No. 71*, p. 26-27.

76 DEWR, *Exhibit No. 25*, p.15.

- Queensland also has specific provisions in relation to unfair contracts. Section 276 of the Qld IR Act, gives the QIRC power to investigate contractual remedies. It includes contracts of service not covered by an industrial instrument, and also independent contracting arrangements;[77]
- In South Australia, there are no unfair contracts provisions in the *Industrial Law Reform (Fair Work) Act 2005*;
- Victoria has referred its workplace relations powers to the Commonwealth and so is covered by the federal legislation which includes unfair contracts provisions;
- In Tasmania, the *Industrial Relations Act 1984* currently contains no deeming or unfair contracts provisions;
- In Western Australia, the *Industrial Relations Act 1979* has no unfair contracts jurisdiction applying to contracts for services; and
- The Australian Capital Territory and the Northern Territory are covered by the WR Act and so are not subject to deeming provisions. The ACT Legislative Assembly recently introduced the Fair Work Contractors Bill 2004. If passed, this Bill will confer an unfair contracts jurisdiction on the ACT Consumer and Trader Tribunal. This provides a less costly option.[78]

Concerns

5.83 There is support for continuing states' and territories' unfair contracts provisions. It was stated that currently unfair contracts reviews are undertaken by the Federal Court, which can be costly and time-consuming.[79] Additionally there is limited applicability given the constitutional constraints and requirement for the independent contractor to be a natural person.[80]

5.84 The Communications Electrical & Plumbing Union (CEPU) stated that by maintaining the state and territory legislation on unfair contracts, costs involved to bring forth any action are reduced and more accessible:

> … [for] ordinary people to take action for unfair contracts where their only avenue of redress is a cost prohibitive Federal Court action[81]

77 DEWR, *Exhibit No. 25*, p.17.

78 DEWR, *Exhibit No. 25,* pp. 15 -20; DEWR-ACT Government, *Exhibit No. 84*, p. 4.

79 DEWR, *Exhibit No. 25,* pp. 15 -20; Prof. A. Stewart, *Submission No. 69,* p. 18; DEWR-ACT Government, *Exhibit No. 84*, p. 4

80 ASU, *Submission No. 53*, pp. 5-6.

81 DEWR-CEPU, *Exhibit No. 48,* p. 8.

5.85 As indicated earlier, independent contractors would have recourse to provisions of the TPA to regulate their commercial relationship.[82] There is overlap with some unfair contract legislation in industrial regulation.

5.86 However, others oppose limiting avenues of redress to trade practices citing concerns of court costs and the need for specialist employment law expertise. NUW state that it is in the interest of all parties to such a contract to have access to a reliable, inexpensive and independent dispute settling mechanism.[83]

5.87 The transport industry raised a number of issues relating to unfair or harsh contractual terms and commercial practices. Concerns include: improper deduction of administrative costs; many hours of unpaid work; breach of contract; and unreasonable restraint of trade provisions.[84] These issues contravene many of the provisions within the TPA.[85]

5.88 Other issues arising from the submissions is that contractors may face restrictive practices, such as demands to sign a union-devised enterprise bargaining agreement (EBA) under Federal/State law, and demands to take out workers' compensation 'top up' insurance, which are employment requirements.[86]

5.89 Another concern falling under the category of 'Unfair Contracts' (Part 4, s. 45 TPA), is the burden of restrictions which may prevent independent contractors working effectively and lead to a competitive disadvantage for employees.[87] This is connected to undercutting.

5.90 Amongst the evidence submitted to the enquiry, the concern about undercutting involved independent contractors and labour hire arrangements. The TWU Victoria/Tasmania stated:

> … the Government should ensure the characterisation of 'employees' and 'independent contractors' allows only legitimate independent contracting to occur, and not as a means of undercutting the comparable safety net rates of pay of employees in an unsafe and unsustainable manner.[88]

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82 *Trade Practices Act*, Part IV, Section 45.

83 NUW, *Submission No. 47*, p. 8.

84 TWU Vic./Tas., *Submission No. 56,* p. 22.

85 Vic. Government, *Submission No. 71,* p. 37.

86 HIA, *Submission No. 61,* p. 8; and further discussed in lesser detail in NSW Government, *Submission No. 35*; pp. 22-23; TWU, *Submission No. 42*, pp. 13-14.

87 HIA, Submission No. 61, pp. 11-12.

88 TWU-Vic./Tas., *Submission No. 56,* p. 23.

5.91 Furthermore, it was considered that undercutting is an act that has a detrimental effect on community standards and expectations. It was stated that independent contractors should meet the same tests as other industrial arrangements so as to not be disadvantaged by the burden of restrictions in comparison to other types of workers.[89]

5.92 The QIRC (s275) commented on undercutting with regard to security guards who were designated as contractors but deemed to be employees by the QIRC bench. This was due to the bench refusing to:

> … send a message that in a competitive industry with very tight margins it is acceptable to deprive workers of entitlements to annual leave, sick leave, long service leave, bereavement leave, family leave, overtime payments, rest pauses, shift allowances, payment for public holidays, penalties for ordinary hours performed on weekends, superannuation entitlements and workcover protection in order to be able to quote lower prices to clients. …
>
> Objectively viewed the Independent Contractor Agreement is designed to avoid the Award and the certified agreement.[90]

5.93 In NSW, evidence submitted to the inquiry from the transport industry expressed concerns in relation to regulation, noting that NSW was the most regulated of all the states and territories.[91] Implications of removing, or interfering with the chapter 6 support mechanisms (of the NSW IR Act) would result in the disruption of over 170 registered contract agreements that 'were freely entered into between owner-drivers and companies which strike an agreed balance … of remuneration and other essential conditions'[92]

5.94 TWU of NSW state that any revision of the current system of industrial relations (section 6, specifically unfair contracts) must maintain the current protection of minimum standards, including a mechanism for guaranteeing remuneration rates not falling below a reasonable 'running' cost.[93]

5.95 However, others in the NSW transport industry state that although the contract determination set minimum rates, undercutting has occurred and now the rate set was sometimes a maximum which was leading to considerable hardship for some independent contractors.

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89 Mr. K. Harvey, ASU, *Transcript of Evidence,* 27 April 2005, p. 66.

90 ALHMWU v Bark Australia [2001] QIRC 22 (28 February 2001); 166 QGIG 254.

91 See NSW RTA, *Submission No. 75,* pp. 5-8; also TWU-NSW, *Submission No. 40,* paras. 19 and 40-41; Ch 6 *Industrial Relations Act 1996* (NSW).

92 TWU-NSW, *Submission No. 40,* pp. 33-34.

93 TWU-NSW, *Submission No. 40,* p. 34.

Alternative conciliation and dispute resolution strategies should be considered. In addition more support for independent contractor owner-drivers and access to business management advice is required.[94]

5.96 It is apparent that there is a lack of consistency in the appropriate legislative approach, trade practices or workplace relations, to respond to contract issues for independent contractors. There is no clear vision on where the boundaries should be set based on the perception and substantive relationship of the independent contractor's position. Business and workers are calling for greater clarity.

Ways forward

5.97 The creation of a consistent national system for the review of unfair contracts has been suggested. However, should this occur the federal legislation should be extended to cover arrangements with contractors who are not natural persons (s 4(1a) of the WR Act) in order to include partnerships and companies to ensure that disguised employment arrangements are limited. [95] (Although it may lead to some confusion as found with this extension beyond natural persons when included with the Freedom of Association provisions in Part XA, WR Act.[96])

5.98 Other possibilities, in addition to amending the TPA or the WR Act or developing independent contractor legislation, are to consider alternative ways to support improved contract negotiation and dispute resolution for independent contractors as small businesses.[97] Giving the Federal Magistrates Court jurisdiction to hear matters relating to unfair contracts would assist. However lower-cost, more user friendly and speedier options need to be considered.[98]

5.99 Victoria provides a recent example. Within owner-drivers in the transport industry there is a high prevalence of contracting and sub-

94 Mr J. Taylor, Courier and Taxi Truck Association, *Transcript of Evidence*, 31 March 2005, p. 45; NSW RTA, *Submission No. 75*, pp. 9-11.

95 Prof. A. Stewart, *Submission No. 69,* p. 18.

96 Vic. Government, *Submission No. 71*, p. 26.

97 *Trade Practices Act 1974* currently prohibits price fixing, certain exclusive dealing, boycotts, abuse of market power, misleading, and false & unconscionable conduct. Section 51 (AC) covers unconscionable conduct criteria for small business transactions.

98 DEWR, *Exhibit No. 25*, p. 20; see also Mr A. Cameron, RCSA, *Transcript of Evidence*, 26 April 2005, p. 27.

contracting arrangements. Approximately 80-85 per cent of owner-drivers within the industry operate as corporations, whilst 15-20 per cent operate as sole traders or partnerships.[99]

5.100 TWU relates experiences that independent contractors have little bargaining power and often confront a 'take it or leave it' behaviour.[100] These types of contracts are provided as 'standard forms' and no alteration is calculated.

5.101 The 'take it or leave it' approach would generally be described as unconscionable conduct, and therefore could be appealed under Section 51 AC of the TPA.[101] It is apparent, however, that the costs and time of accessing courts dissuade contractors from regularly using this remedy.

5.102 The NSW Road Transport Association (RTA), through a survey of their members, has expressed interest in alternatives to the present system, namely a system whereby mediation as a method of dispute resolution is present, and in some cases, the common law.[102] One possibility raised with the Committee is the proposed Victorian *Owner Drivers and Forestry Contractors Bill 2005* (Owner Drivers Bill). The TWU, in representation of owner-drivers, also support alternatives to the current system.[103]

5.103 The Owner Drivers Bill takes an alternative approach to self-employed workers and small businesses. The policy approach adopted in the Owner Drivers Bill does not apply a labour law styled-solution to owner-drivers; instead it deals with them within a framework of commercial and fair trading laws. It is modelled on the *Retail Leases Act* 2003 (Vic), which is stated as successfully addressing similar issues of market failure. [104]

5.104 The Owner Drivers Bill can be summarised as:

- not altering the legal status of the contractors as small businesses;

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99 NSW RTA, *Submission No. 75,* p. 2; TWU-NSW, *Submission No. 40,* p. 3. However, across all the total transport and storage sector approximately 72 per cent of workers are employees. Waite, M and Will, L, 2001, *Self-employed contractors in Australia: incidence and characteristics*, Productivity Commission Staff Research Paper, p. 48.

100 TWU-Federal, *Submission No. 42*, p. 10.

101 ACCC, 2004, *Guide to unconscionable conduct*, accessed 20 June 2005 <www.accc.gov.au/content/item.phtml?itemId=544299&nodeId=file42310ef82b432&fn=UnconscionableConduct_Oct2004.pdf>.

102 NSW RTA, *Submission No. 75,* p. 9.

103 Mr W. Noonan, TWU, *Transcript of Evidence,* 27 April 2005, p. 27; also discussed to a lesser degree in Prof. A. Stewart, *Submission No. 69,* p. 2.

104 Vic. Government, *Submission No. 71,* p. 9.

- containing a broad definition of owner-driver to cover all forms of small business structures, including businesses that employ other workers;
- dealing with these small businesses within a framework of commercial laws and institutions, rather than industrial laws and institutions;
- focussing on the identified market failure of information imbalance, requiring provision of information to owner-drivers on typical business overhead costs and on small business skills;
- not prescribing or regulating commercial terms, with the exception of requiring a minimum period of notice of termination;
- providing for alternative dispute resolution based on existing business-to-business trading laws; and
- allowing for the appointment of agents to conduct contractual negotiations and allows for joint negotiations by groups of owner-drivers or forestry contractors with their single hirer.[105]

5.105 The Owners Drivers Bill also allows for codes of practice to be developed on commercial conduct. Codes can be made regulations after advice from Industry Councils comprising representatives of all industry interests.[106]

5.106 The Owner Drivers Bill bears a close relationship to the TPA, in that it imports the powers under unconscionable conduct, and sections relating to disputes between traders of the *Fair Trading Act 1999* (Vic), and adds in a process of mediation by a Small Business Commissioner.

5.107 Further requirements to this Bill include: contracts to be in writing; provisions for disclosure of certain information to contractors; and prohibition of certain harsh and oppressive practices.

5.108 However, the Victorian Association of Forest Industries argues that the Owner Drivers Bill will result in codified and regulated contracting that is anti-competitive in business to business arrangements.[107]

5.109 Therefore a balance needs to be sought between additional regulation, providing some protection for independent contractors, and still ensuring competitive practices.

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105 Vic. Government, *Submission No. 71,* p. 9; Owner Drivers and Forestry Contractors Bill 2005.

106 Vic. Government, *Submission No. 71,* pp. 9-10.

107 Vic. Association of Forest Industries, *Submission No. 76*, p. 2.

5.110 Additional support for increased information was also advocated by the farming industry. NFF supports improved contracting documentation and has produced the 'NFF Kit' which details farmers' regulatory obligations when hiring contractors. [108]

5.111 The NFF kit highlights the difficulties and variations across jurisdictions in dealing with contractors and labour hire firms. The kit explains the rights and obligations on the farmer when engaging independent contractors and provides a basic template contract. It offers a questionnaire which aids in determining the control test (i.e. whether they are an employee or a contractor). It also offers a contact list of relevant state organisations (such as workers' compensation, taxation, superannuation, immigration, award wages and OH S).[109]

Committee view

5.112 The Committee considers that there are some advantages to the approach proposed by the Owner Drivers Bill. One benefit is the broader view of independent contractors as including a business structure, rather than being limited to natural persons.

Recommendation 12

The Committee recommends that the Australian Government broaden the description used in the *Workplace Relations Act 1996* of an independent contractor and extend it beyond 'a natural person'.

5.113 The Committee is aware of the role that ACCC plays in assisting small business and their rights under trade practices. [110] Additionally the Australian Government Office of Small Business builds and maintains links with small businesses and their representative organisations and examines critical factors influencing the growth of small firms and the small business sector generally.[111]

5.114 However, there appears to be an opportunity to specifically target independent contractors to identify their information needs and

108 The kit can be found in: NFF, *Submission No. 39,* Attachment B.

109 NFF, *Submission No. 39,* Attachment B.

110 See for example publications such as ACCC, 2004, *Small Business and the Trade Practices Act*, accessed 30 June 2005, <www.accc.gov.au/content/index.phtml/itemId/304583>.

111 Department of Industry, Tourism and Resources, *Office of Small Business – what we do*; accessed 30 June 2005, < http://sblegal.industry.gov.au/contactus.asp>.

develop appropriate legislation suited to their requirements at the smallest end of business arrangements.

Recommendation 13

The Committee recommends that the Australian Government Office of Small Business collate and further develop a series of resources for independent contractors. Collated resources should provide assistance on:

- **setting up a small business;**
- **financial and reporting requirements;**
- **dispute resolution options; and**
- **business management practices.**

5.115 The Committee considers that further supporting the commercial nature of independent contracting is the most appropriate course of action, along with additional strategies to provide better support and access to dispute resolution. Independent contractors would have recourse to provisions of the TPA to regulate their commercial relationship.[112]

5.116 It is noted that there is dissent within the Committee on this approach.

Recommendation 14

The Committee recommends that the Australian Government incorporate the following protections when drafting legislation for independent contractors:

- **preserving the legal status of independent contractors as small businesses;**
- **providing a broad description of independent contractor to cover all forms of small business structures;**
- **regulating independent contractors as small businesses within a framework of commercial laws and institutions, rather than industrial laws and institutions; and**
- **providing alternative dispute resolution procedures.**

112 *Trade Practices Act*, Part IV, Section 45.

Artificial business relationships

5.117 Continuing the theme of the chapter of commercial arrangements and business structures, consideration will now be given to where questions have been raised about the legitimate nature of some working relationships.

5.118 Methods identified by which employers can avoid an employment relationship include:

- manipulating the indicia of employment;
- hiring labour through an agency; and
- interposing another kind of entity such as
  - ⇒ tertiary beneficiary trusts,
  - ⇒ partnership arrangements,
  - ⇒ corporations, and
  - ⇒ franchises.[113]

5.119 Arrangements relating to labour hire, manipulating the indicia of employment to craft a finding of independent contractor, and incorporation will be discussed in the following sections.

Labour hire arrangements

5.120 Chapter 4 outlines some of the concerns with using labour hire arrangements, such as skills development, OHS and employment conditions. It has been stated by Job Watch that using labour hire also removes the responsibility for unfair dismissal from the host business to the labour hire agency. A termination of employment is required in order to lodge an unfair dismissal claim against the labour hire agency.[114]

5.121 However, if the worker does not gain further work at the host business or through the labour hire agency, it is difficult to substantiate that a termination has occurred. The triangular relationship prevents a claim being made against the host business.[115]

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113 Qld Government, *Submission No.66,* pp. 6, 30-31. Law Council of Australia, *Submission No. 59,* p. 2. In Tertiary Beneficiary Trusts workers are treated as beneficiaries and paid dividends rather than wages. Greater regulation of franchising arrangements occurred with the introduction of the franchising code of conduct under the TPA referred to in the previous chapter.

114 Job Watch, *Submission No. 23*, pp. 11-12.

115 Job Watch, *Submission No. 23*, pp. 11-12.

5.122 A Western Australian example indicated that in some instances labour hire arrangements may be being used inappropriately.[116] Evidence was heard from a labour hire worker who had worked regular shift hours for 11 years with a host business. Over this time the worker did not receive any of the leave entitlements of a direct employee and, when their hours were reduced without consultation, they had no recourse due to the nature of labour hire placement – despite the expectation of ongoing employment and the length of service with the host business.[117]

5.123 It has been reported that the use of this triangular relationship, to avoid a finding of an employment relationship for other reasons, also occurs in contractor placement services, such as 'Odco' style arrangements.[118] Therefore, the following section on independent contracting would also apply to these arrangements.

Independent contracting and business structures

5.124 There is widespread in principle support for genuine independent contracting. However, the use of 'sham' or artificial contract arrangements to hide a genuine employment relationship is not condoned by governments, business groups or worker representatives.[119] Strong views were presented to the Committee on the need to curb such arrangements.

5.125 It was stated that the use of independent contractor arrangements has changed from meeting specialist skills needed for a period of time, such as licensed plumbers or electricians, to employers engaging an entire workforce on what were considered by one union to be sham contractor arrangements.[120] They state that, as a result, workers are taken outside of the industrial relations system, and deprived of the benefits and protections associated with being defined as an employee under relevant industrial laws.

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116 Ms J. Freeman, UnionsWA, *Transcript of Evidence*, 20 May 2005, p. 45.

117 Ms J. Freeman, UnionsWA, *Transcript of Evidence*, 20 May 2005, p. 48; AMWU, *Submission No. 46*, p. 26.

118 Prof. A. Stewart, *Submission No. 69* p. 20.

119 For example Qld Government, *Submission No. 66*, p. 3; CFMEU – Mining & Energy Division, *Submission No. 18*, p. 9; NFF, *Submission No. 39*, p. 9; DOCEP – WA Government, *Submission No. 33*, p. 1.

120 NUW, *Submission No. 47*, p. 3.

What is a 'sham'

5.126 Concerns about independent contracting arrangements are not limited to the narrow definition of 'sham' arrangements; there are also disguised employee or artificial contracting arrangements. One reasonably limited definition of 'sham' was offered by the Victorian Government:

> The term "sham" is used to describe an *attempt* by parties to disguise what is in law an employment relationship as a contracting relationship. "Sham contracting" is thus a narrow concept.[121]

5.127 Professor Stewart continues this view in his submission, where he states:

> It is only a sham when parties construct what they would both understand to be an employment arrangement and then try and disguise it as something else by adopting an arrangement that does not genuinely reflect their intentions.[122]

5.128 DEWR describe sham arrangements are where employers seek to conceal employment relationships to appear as independent contracting arrangements in order to avoid responsibility for some legal entitlements payable to employees.[123]

5.129 DEWR stated that there is difficulty in estimating the prevalence of sham contracting:

> It is going to be very difficult to estimate the incidence of sham arrangements for the same sorts of reasons that it is hard to estimate the size of the black economy. By their nature, they are deceptive arrangements that look like an independent contracting arrangement but are, in fact, an employment relationship, so trying to identify those in any sort of systematic way from surveys or ABS statistics or those sorts of sources is going to be very difficult. Probably the best examples we have are examples that have come to light through legal proceedings.[124]

5.130 A broader view of sham arrangements included evidence from a union body on the problematic nature of sham, or 'bogus' independent contracting arrangements.[125] Where employers classify

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121 Vic. Government, *Submission No. 71*, p. 34.

122 Prof. A. Stewart, *Submission No. 69,* p. 7.

123 DEWR, *Exhibit No. 25,* p. 22.

124 Mr B. Pridmore, DEWR, *Transcript of Evidence*, 16 June 2005, p. 32.

125 CFMEU, *Submission No. 5,* p. 4.

their workers as sub-contractors, they are able to avoid award entitlements, and are described as 'disguised employment'. In the building and construction industry, CFMEU state that sham arrangements are widespread. In their view the result is: workers with lower overall remuneration; undercutting of honest employers; and loss of revenue to the Australian Government and the community.[126]

5.131 The CFMEU believe that by forcing workers into bogus subcontracting, it has the effect of creating large numbers of tax evaders, 'weak legislation has the effect of generating a positive incentive for tax evasion'.[127]

5.132 Furthermore, they state it is this relationship of cost-saving and tax-savings that has allowed the sham arrangements to thrive. Tax minimisation or avoidance will be discussed in a later section.

5.133 The Department of Consumer and Employment Protection (DOCEP) in WA argue that there is no evidence to suggest a high incidence of sham arrangements in the building and construction industry. However, there appears to be an increasing trend in the number of complaints received regarding sham arrangements in the service industry, such as hospitality, retail, aged care, clerical and security.[128] It was revealed that in these cases, true employment relationships existed but were concealed under the guise of independent contracting.

5.134 The avoidance of legal entitlements, including tax evasion and remuneration issues, is not the only concern expressed in the submissions. Lack of training, safety issues and economic insecurity on behalf of the independent contractor were also issues identified.[129]

5.135 On the surface, it was submitted that sham independent contracting may appear appealing to the worker. Often the worker is paid cash in hand, and the earnings remain undeclared.[130]

5.136 Evidence indicates that many workers are not aware of the practical implications of working as an independent contractor, which may hinder their ability to make informed choices.[131]

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126 CFMEU, *Submission No. 5,* p. 4.

127 CFMEU, *Submission No. 5,* Appendix 9: CFMEU submission to Inquiry into Structure and Distributive Effects of the Australian Taxation System, p. 2.

128 DOCEP-WA, *Submission No. 33*, p. 2.

129 ACTU, *Submission No. 60*, pp. 18-19; AMWU, *Submission No. 46*, pp. 32-33, 57-60.

130 CFMEU, *Submission No. 18,* pp. 2-3.

131 DOCEP-WA Government, *Submission No. 33,* p. 1.

5.137 There is nothing inherently wrong with an independent contracting arrangement, if both parties freely enter into it with a proper understanding of the nature and effects of such a relationship.[132] However, a typical example provided to the Committee relates to young workers in marginal employment, who are required to sign agreements to become contractors.

5.138 The issue raised is the lack of independence, and if the worker is inexperienced they may not appreciate that what they are agreeing to is transferring responsibility from the employer to the individual worker for issues such as payment of:

- tax;
- superannuation;
- workers' compensation insurance; and
- public liability insurance effectively making them liable for any damage to property.[133]

5.139 However, if the contract is wholly or principally for labour then the employer still has obligations. ATO advised that they have an employer obligations program where employers are visited to ensure they fulfil their obligations in relation to PAYG withholding and superannuation.[134]

5.140 One example of transferring responsibility, offered by Unions NSW, occurred in 2000 at the Olympic Stadium. A multinational catering company working in a major Olympic venue tried to avoid paying award wages to its catering employees, some who were as young as 15 years old, by attempting to turn them into independent contractors.

> Parents of some of the employees contacted Unions NSW to complain that their children were being required to take out an A.B.N. and would only be paid on a commission basis. This arrangement was contrary to an advertisement placed in many regional newspapers to lure workers during the Olympic games and contrary to an Industrial Award, which applied to the Employer.[135]

5.141 This example highlights that some workers may be exploited by business, and the usefulness of representation or ensuring sufficient

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132 NSW Government, *Submission No. 35*, p. 4.

133 Qld Government, *Submission No.66,* p. 30.

134 Mr T. Sullivan, ATO, *Transcript of Evidence*, 16 June 2005, p. 17.

135 Unions NSW, *Submission No. 44,* pp. 11-12; Unions NSW, *Exhibit No. 37*: Copy of correspondence regarding minors and independent contracting.

investigatory resources are available to assist in helping to resolve the issues.[136] A second example can be drawn on to emphasize the vulnerability of workers in the workplace when there are not sufficient safeguards to protect their rights.

5.142 In this example, a Salvation Army client, with a mild intellectual disability and on Disability Support Pension (DSP) for four years, has worked part-time as a cleaner since October 2004. The client informed Centrelink each fortnight of her income, and they adjusted her DSP accordingly. The client is concerned about not paying tax, as the employer is not deducting the tax from her earnings.[137]

5.143 The cleaning agency informed the client that she was a sub-contractor as she had signed a contract stating the arrangement. The client did sign a contract; however she had no idea what it meant for her employment. She receives a weekly pay, and does not invoice the agency. She is offered work on a weekly basis; however, she does not have regular customers of her own.

5.144 It was made clear to the Salvation Army that some cleaning agencies were moving to sub-contractors rather than employees in the hope of avoiding responsibilities in regard to workers' compensation, superannuation, pro-rata long service leave and holiday pay. The client was to apply for an ABN; however, it was stated she did not understand the implications this would have on her rights as a worker or her possible taxation debts.[138]

5.145 The implications for the contractors are that they are limited in their avenues of recourse. There are anti-avoidance provisions in tax law; however, this does not help the contractor in relation to the other issues such as superannuation guarantee,[139] workers' compensation and other legal requirements for which the principal business may be responsible.

5.146 For the purposes of the superannuation guarantee, for independent contractors even if an ABN is quoted they may be considered an employee. However there is no obligation if the contract is with a company or partnership, nor if the person contracted is engaged to

136 DOCEP- WA Government, *Submission No. 33*, p. 1.

137 Salvation Army, *Submission No. 68,* p. 1.

138 Salvation Army, *Submission No. 68,* p. 1.

139 Even in the federal arena, it was found that two thirds of Commonwealth agencies audited did not meet their superannuation obligations for independent contractors when contracts were wholly or principally for labour. This was thought in the main to be a lack of awareness of obligations; ANAO, 2004, *ANAO Audit Report No. 13 2004-05, Superannuation payments for Independent Contractors working for the Australian Government*, pp. 12-13.

produce a result or is free to engage other people to perform the work.[140]

5.147 Further areas of interest include the genuine doubt about employment status because of the nature of the working relationship. This can happen where self-employed workers gradually enter into permanent arrangements with a single client,

> … where persons are recruited and work at a distance without fixed hours or days, have special payment arrangements, but still follow instructions and are subject to control.[141]

5.148 The broader view of 'sham' arrangements assumes the creation of business structures to avoid employment obligations. Strategies for investigation and possible remedies are included in the next chapter.

Incorporation

5.149 Evidence from the submissions to the inquiry indicates that employers often dictate the nature of the contractual dealings, and that the workers often do not have the bargaining power to influence the result. In some instances the control extends to the employer requiring contractors to incorporate, or use a company as a trading entity. The Victorian Government believes this to be:

> … motivated by a desire to avoid existing Federal unfair contracts laws and to avoid the statutory and common law regulation and costs associated with a finding of employment.[142]

5.150 The Law Council note that:

> It is also established law that a company or partnership cannot usually be classified as an employee. In the transport industry, for example, it is common practice for owner-drivers to be incorporated.[143]

5.151 The TWU Vic/Tas branch supports this view that owner-drivers operate either as sole traders, partnerships or as incorporated companies. They state that in the past 10 years there has been a

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140 ATO, *Superannuation guarantee-employer obligations*, accessed 24 May 2005, <www.ato.gov.au/super/content..asp?doc=/content/19136.htm>.

141 Qld Government, *Submission No.66*, p. 30.

142 Vic. Government, *Submission No. 71,* p. 34.

143 Law Council of Australia, *Submission No. 59,* p. 2.

substantial increase in the number of owner-drivers operating as incorporated companies.[144]

Implications

5.152 The implications for independent contractors who are incorporated are the additional costs of maintaining a corporate entity. However, there are tax advantages with payment of the corporate tax rate rather than the individual rate as long as they meet the personal service business requirements.[145] (Refer to the next section.) This indicates the incentive for independent contractors/employees to move over to a company entity.[146]

5.153 In addition, Division 84 of the Income Tax Assessment Act 1997 provides for deductible business expenses for contractors, based on them operating a Personal Services Business. A person must be a contractor at common law to be eligible.[147] However, the extra costs of superannuation, workers' compensation and/or insurance, and leave need to be taken into consideration.

5.154 The hirer (principal contractor) is not required to make superannuation contributions for incorporated contractors, and in Victoria, the hirer (principal contractor) is not obliged to make payments of workers' compensation premiums.[148]

> The significant financial savings achieved to the benefit of hirers and the detriment of the workers that result from incorporation have prompted a significant trend among the hirers of labour to require contractors to be incorporated.[149]

5.155 Furthermore it is noted that, in Victoria under Commonwealth legislation, contractors who incorporate do not have standing to make an application under the unfair contracts section, ss.127A-C, of the WR Act. 'This provision has contributed to a trend towards incorporation.'[150]

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144 TWU-Vic./Tas., *Submission No. 56,* p. 6.

145 For example company (general) tax rate is a standard 30% (2003-2004); individual taxable income $21,601 -$58,000 = 30%; $58,001 - $70,000 = 42%; over $70,000 = 47%, accessed 17 June 2005 <www.ato.gov.au/print.asp?doc=/content/12333.htm>; and <www.ato.gov.au/businesses/content.asp?doc=/content/44266.htm>.

146 DEWR-Ms R. Bremers, *Exhibit No. 44*, p. 2.

147 HIA, *Submission No. 61*, pp. 5-6.

148 Vic. Government, *Submission No. 71,* p. 17.

149 Vic. Government, *Submission No. 71,* p. 17.

150 Vic. Government, *Submission No. 71*, p. 38.

5.156 The Victorian Government observes that the Federal Government's Small Business Deregulation Taskforce noted this was a common practice.

5.157 Increasing numbers of larger businesses require small businesses and independent contractors to incorporate so that those contracting their services are able to avoid the costs that flow from deeming provisions.

> Where small businesses accede to this requirement, additional compliance costs are inevitable. In these situations, the regulations are working against the viability of small businesses and dictating the structure of their business arrangements.[151]

5.158 As highlighted in an earlier section, expanding the description of independent contractors beyond only natural persons under the unfair contracts provisions, ss. 127A-C, of the WR Act may diminish the pressure from employers to avoid federal legislation under unfair contracts provisions.

5.159 The Committee considers that this may have the effect of reducing the incentive to re-structure business arrangements where the demands of the trade do not require it, and therefore lessen the additional costs to the independent contractor.

Tax minimisation

5.160 As discussed earlier in the report the introduction of legislative measures in 2000 to limit tax avoidance relating to independent contractors has mainly focussed on personal services income.

> Most of the contractors who work through any of our licensed agencies are sole traders or individuals, so PSI does not come into the equation. PSI is really a tax avoidance issue for businesses that structure into entities and try to divert income that they have earned from personal services through a corporate tax rate.[152]

5.161 Income tax law requires businesses to withhold tax on payments to both employees and contractors through the PAYG system. If a labour hire firm acting as a principal contractor supplies workers, the business pays the labour hire firm, not the workers. The business is

151 Commonwealth Small Business Deregulation Taskforce *Time for Business: Report of the Small Business Deregulation Taskforce*, November 1998, p. 51 cited in Vic. Government, *Submission No. 71*, p. 35.

152 Ms J. Meinen, Labour Force Australia, *Transcript of Evidence*, 26 April 2005, p. 74.

not required to withhold tax from payments made to the labour hire firm, unless it does not quote its ABN.[153]

5.162 However, if the business is a labour hire firm, like any other employer they must withhold tax from any payments made to individual workers.

5.163 Personal services income is income that is earned by the personal efforts or skills of an individual. This income can be 'alienated' when an entity (a company, trust or partnership) is interposed between the individual and the person paying for their services, so that the interposed entity derives the income rather than the individual.

5.164 The income may be split with other members of the interposed entity or retained within the interposed entity, allowing less tax to be paid or the tax liability to be deferred.[154]

5.165 AMWU also cited concerns with independent contractors' tax arrangements and the creation of other entities.

> On the impact on the Commonwealth revenue, in a study by the National Institute of Economic and Industry Research for the union, NIEIR concluded that growth in contracting is leading to a $14.38 billion per annum risk to the tax base. Most independent contractors are in fact dependent contractors or employees. The loss in the tax base is a mixture of tax evasion and tax avoidance, including the failure to report substantial amounts of income, claims for fictional or improper deductions and the ability to split income with families and relatives and lower the average tax rate. As you see in our submission, sole traders claim that 8.96 per cent of their business income is spent on motor vehicle expenses, in contrast to the average construction company who claim 2.84 per cent.
>
> Partnerships in the manufacturing industry claim on average 66.21 per cent of their income as 'other expenses' compared to a manufacturing company standard of 48.74 per cent. In the finance and insurance industries, sole traders claim 2.04 per cent of their income as payments to related entities. This is likely to be income splitting so that the tax base is reduced by half.[155]

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153 ATO, *Determine the status of your workers*, accessed 21 June 2005 <www.ato.gov.au/businesses/content.asp?doc=/content/35887.htm>.

154 The Treasury, *Submission No. 73*, p. 2.

155 Mr D. Cameron, AMWU, *Transcript of Evidence*, 31 March 2005, p. 69.

5.166 PSI legislation acts to address these issues by preventing individuals from claiming to be businesses in order to avoid paying income tax at individual rates. It does not affect individuals who are genuinely in business.[156]

5.167 In 2001, the Government introduced self-assessment to determine whether individuals are independent contractors against the 'results test'. If the results test is passed, the taxpayer is not affected by the alienation measures regardless of the proportion of their income derived from a single source.

5.168 To satisfy the 'results test' the individual must:

- work to produce a result; and
- provide plant and equipment or tools of the trade (if required); and
- be liable for rectification of any defects in work performed.

5.169 If individuals cannot meet the results' test then the 80 per cent rule and personal services business tests are used to determine business status.

5.170 The intent of the provisions is to achieve consistent taxation treatment for personal services income irrespective of the structures in places to receive that income. Additionally, the law does not impinge on any commercial or contractual obligation between parties affected by the measures and does not impact on genuine business undertakings.[157]

Compliance with PSI

5.171 However, Professor Stewart outlines a lack of faith (due to a lack of resources) in the compliance audit program related to alienation of personal services income which checks that contractors are correctly reporting.[158]

5.172 ATO reports that of taxpayers seeking to be considered as a personal service business, 75 per cent self assess under the results test. The remainder use a combination of the 80/20 rule, unrelated clients, business premises or employment tests. (One per cent or less have personal service business determinations from the Commissioner of Taxation.)[159]

5.173 ATO indicated that of the over 550 compliance audits undertaken in this area, approximately one third required adjustments. The main

156 The Treasury, *Submission No. 73*, p. 2.

157 The Treasury, *Submission No. 73*, p. 2.

158 Prof. A. Stewart, *Submission No. 69*, pp. 8-9.

159 The Treasury, *Submission No. 73*, p. 3; Mr M. Konza, ATO, Transcript of Evidence, 16 June 2005, p. 8.

industries the ATO focussed on were those contractors working through labour hire firms generally in information technology (IT) and building and construction. ATO indicated that they believed that the legislation has had the desired effect and they are now receiving fewer inquiries and are beginning to divert their resources to other areas of greater compliance need.[160]

5.174 However, the anti-avoidance provisions in Part IVA of the Income Tax Act may still apply to personal service business. Therefore, ATO is conducting a test case program to clarify the application of Part IVA.[161]

Proliferation of Australian Business Numbers

5.175 The construction industry has a high proportion of independent contracting arrangements. The Civil Contractors Federation (CFF) comments on the need for tighter regulation of independent contractor status.[162] They state that the use of ABNs in the construction industry as a proxy for contractor status is inadequate with a proliferation of sub-contractors.

5.176 Additionally, the CFMEU states that ABN applications need to be scrutinised more thoroughly.[163] The application for the issuing of business numbers is basically self assessment. All the ATO will verify is: first, that the person does not already have an ABN; and, second, the identity of the person.

5.177 ATO responded that an ABN is expected to be delivered to a business within 10 working days. This does not allow significant checking time. However, if the description of the business and the registration look questionable then they will be queried.[164]

5.178 The ATO also outlined the difficulties in linking requests for ABNs through the Australian Business Register with current employment status and work site.[165] An individual's tax file number is required if the business structure is as a sole trader. However, if the business

160 The Treasury, *Submission No. 73*, p. 5; Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, pp. 3, 6.

161 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, p. 3.

162 CCF, *Submission No. 15*, pp. 7-9.

163 CFMEU, *Submission No. 5,* Appendix 9, p. 1.

164 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, p. 9.

165 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, pp. 9-10.

structure to be established is as a company then a new tax file number will be sought.[166]

5.179 Given that building contractors are involved in an industry which usually meets the results test,[167] and that they often work at multiple sites, then it would appear that in the main that independent contractor status for tax purposes (i.e. as a personal service business) would be legitimate.

5.180 Other industries also raised concerns. For example workers in the IT industry state that the results test is biased against professionals.[168] ATO acknowledge that they do focus on the IT industry because IT contractors, programmers for example, are not generally paid to deliver a completed product, but are paid on an hourly basis. This would then suggest that they do not meet the results test.[169]

5.181 The effect of issuing ABNs impacts on the withholding of taxation. ATO cautions that just because a worker quotes an ABN does not mean that they are an independent contractor. Whether a worker is an employee or an independent contractor depends on all the facts and circumstances of how a business engages the worker.[170]

5.182 However, HIA states that withholding obligations do not necessarily apply when the taxpayer is a contractor who quotes an ABN.[171] Most independent contractors provide for their tax obligations through the PAYG instalments system.[172]

5.183 ATO stated that they had worked with a range of industry groups and unions to develop information sheets and provide advice to the industry sector to support the changes that were introduced with the personal service income legislation. These included organisations in the building and construction industry, ICA, RCSA, APESMA and the transport industry.[173]

5.184 However, Labour Force Australia commented on the interaction between the labour hire sector and contractors, and stated that some

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166 ATO, *Registering your business*, accessed 29 July 2005, p. 2, <www.ato.gov.au/print.asp?doc=/content/25316.htm>.

167 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, pp. 10-12.

168 DEWR-Ms R. Bremers, *Exhibit No. 44*, pp. 1-2;

169 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, p. 6.

170 ATO, *Determine the status of your workers*, accessed 21 June 2005, <www.ato.gov.au/businesses/content.asp?doc=/content/35887.htm>.

171 HIA, *Submission No. 61*, pp. 5-6.

172 ATO, *PAYG withholding guide no 2 - How to determine if workers are employees or independent contractors,* accessed 21 June 2005, <www.ato.gov.au/businesses/content.asp?doc=/content/4540.htm>.

173 Mr M. Konza, ATO, *Transcript of Evidence*, 16 June 2005, p. 3.

independent contractors were not clear on the requirements of taxation legislation:

> When the tax law changed to PAYG in 2000 it specifically included a section for labour hire but did not discriminate whether it was employment or contracting. The tax requirement, as it relates to labour hire, is that PAYG is deducted from individuals and sole traders regardless of whether they have an ABN or GST registration.[174]

5.185 The Committee is concerned that if a business requests former employees to register for an ABN and then regard them as contractors this situation does not take into account the legalities of the common law distinction, unless other changes to working arrangements are made.

5.186 Additionally, this situation may lead to confusion, tax liabilities for the contractor and the loss of revenue for the Australian Government. The business is reducing their liabilities and not correctly withholding or reporting. Additionally independent contractors in this situation may not be aware of their changed tax obligations.

5.187 The Committee considers that additional strategies are still needed to ensure that independent contracting arrangements are legitimate.

In summary

5.188 Deeming as a device to provide protection for workers with lesser bargaining power has been used by a number of states, across a range of legislation. The advantages and disadvantages have been discussed.

5.189 The concept of independent contracting as a commercial relationship was raised in evidence. Suggestions were made to use unfair contract provisions in the TPA and the WR Act to further strengthen or customise support for independent contractors. An alternative legislative approach proposed in Victoria with the owner-drivers was considered.

5.190 Artificial independent contracting arrangements were reviewed. There is great difficulty in quantifying the incidence of sham and disguised employment arrangements. The trend for incorporation as a business structure was discussed, followed by concern raised regarding tax minimisation strategies.

174 Ms J. Meinen, Labour Force Australia, *Transcript of Evidence*, 26 April 2005, p. 74.

5.191 The next chapter will consider the future role of labour hire and independent contracting arrangements. Strategies to pursue national consistency and legitimacy in labour hire and independent contracting will build on material presented in earlier chapters.