

Operations Manual Supplementary Information Relating to Sham Contracting

7.4 Confirming the employment or contractor status

Defining the status under which an individual (usually the complainant) is engaged needs to be considered by the Fair Work Inspector. Confirming whether a complainant is an employee or a contractor provides the FWO with the means to determine whether or not any contraventions have occurred under the relevant legislation.

While it is true that only a court is able to conclusively determine the status of a person's employment, as a matter of practical necessity the Fair Work Inspector will likely form a view early in the investigation as to whether the relationship is one of employment or contracting.

7.4.1 Employees

Broadly, employees are engaged under an employment contract also known as a 'contract of service' (which need not be in writing), and are generally subject to a high degree of control by their employer. Their tenure is usually regular and ongoing, and their employers are obliged to comply with employment laws providing for entitlements such as wages, leave and superannuation.

The [FW Act](#) makes many references to employees, and distinguishes between the term "employee with its ordinary meaning" and a "national system employee." Under the [FW Act](#) certain provisions apply to all employees (i.e. an employee with its ordinary meaning), while others only apply to national system employees.

An "employee with its ordinary meaning" is defined in s15 of the [FW Act](#) which states that:

"A reference in this Act to an employee with its ordinary meaning:
(a) includes a reference to a person who is usually such an employee
(b) does not include a person on a vocational placement."

A national system employee is defined in s13 of the [FW Act](#) as:

"an individual so far as he or she is employed, or usually employed, as described in the definition of national system employer in section 14, by a national system employer, except on vocational placement."

The [FW Act](#) (in s12) further provides that:

"employee is defined in the first Division of each Part (other than Part 1-1) in which the term appears."

Accordingly, a Fair Work Inspector will need to confirm during the investigation:

- whether the complainant is an employee with its ordinary meaning (refer s15 of the [FW Act](#))
- whether the complainant is a national system employee (refer ss 13 and 14 of the [FW Act](#))
- whether the entitlement claimed by the complainant is provided to all employees, or only to national system employees, under the relevant part of the [FW Act](#).

7.4.2 Contractors

An independent contractor is engaged under a 'contract *for services*'. A contract for services is a commercial contract with working arrangements which differ from those of an employee in a variety of ways. Contractors are generally said to run their own business and may operate their own company, and they are not usually subject to direction or control. The contractual arrangement is entered into between the principal and the independent contractor.

The [FW Act](#) does not provide a definition of an independent contractor, other than to note that the term "independent contractor is not confined to an individual" (s12). There is also no definition of contractor provided in the *Independent Contractors Act 2006* (Cth) ([IC Act](#)).

7.4.3 Indicators for determining employment status

In assessing whether a worker is an employee or a contractor, the Fair Work Inspector should be guided by the various factors commonly considered by the courts in previous cases, referred to as the multi factor test. This test can assist the Fair Work Inspector to form a view based on the information available, so that the matter can be actioned. In assessing the particular status of a worker the Fair Work Inspector will need to consider each case on its own merits.

The following factors have been taken into account by the courts in determining whether a person is an employee or an independent contractor.

- control
- terms of the contract
- method of remuneration
- provision of equipment
- obligation to work
- hours of work and leave
- deduction of income tax
- ability to delegate work
- ability to perform work for others
- risk.

7.4.4 Background to the multi factor test

The multi factor test operates by looking at the total relationship between the parties. Fair Work Inspectors should note that ***no single issue*** concerning control, economic independence or the description of the relationship in a contract will be determinative. For instance, if a complainant is found to have an ABN, this is not sufficient enough to make a determination that the complainant is a contractor. Courts will, however, place greater weight on some matters, in particular, on the right to control the manner in which the work is performed.

Previously, the High Court decision of [Stevens v Brodribb Sawmilling Company Pty Ltd \(1986\) 160 CLR 16](#) was often cited when courts considered such matters. More recently, the High Court in [Hollis v Vabu Pty Ltd \(2001\) 207 CLR 21](#) emphasised the need to look at the totality of the relationship between the parties and be primarily guided by whether, in a practical sense, the worker can be said to be "running their own business or enterprise".

The Fair Work Inspector will no doubt find several cases published each year that address this issue, and that reach distinct conclusions, based on the evidence placed before the courts.

However, the Fair Work Inspector is not expected to be proficient in case law, and should seek the advice of their team leader, principal investigator, or Legal Group as needed (see also 7.4.8 below).

7.4.5 Where the relationship is defined in the written contract

Fair Work Inspectors will investigate cases where a written contract between the parties stipulates that the relationship is one of a “contractor.” However, one of the parties to the contract (usually the complainant) may dispute this description and allege that in actuality the relationship is one of employer and employee, despite the wording of the contract. Fair Work Inspectors should remain alert to the potential that the matter may involve issues of “sham contracting” as well as the alleged underpayment.

Again, in such cases the Fair Work Inspector will need to consider that the written contract is only **one** factor to be considered. In assessing whether a worker is an independent contractor or an employee a Fair Work Inspector should look not only at the contractual agreement between the parties but at the practical realities of the arrangements, to determine the factual relationship that exists between the parties.

If there are clear indications that the actual relationship is different to that specified in the contract (i.e. that the complainant is an employee), then the Fair Work Inspector should proceed with the investigation on that basis.

7.4.6 Where state or other laws deem the person to be a contractor or employee

An individual may be called a “contractor” according to certain laws (e.g. they may be described as a contractor for taxation purposes). However, this does not automatically exempt them from employee provisions of the [FW Act](#) or make them a contractor under the IC Act. Under the multi factor test (see 7.4.3 above), it may be found that the person is in fact an employee.

Similarly, some state laws may treat or deem contractors to be employees for certain purposes, such as workers’ compensation. This does not necessarily make them an employee under the [FW Act](#) or exempt them from coverage under the IC Act. The multi factor test must be used by the Fair Work Inspector to ascertain the true nature of the relationship.

7.4.7 Making an assessment

As noted above, early in the investigation, the Fair Work Inspector will need to assess whether there is an employment relationship or contracting arrangement in place, using the multi factor test (see 7.4.3 above). When questioning the complainant, Fair Work Inspectors should use the Compliance Tool Notional Employee/Contractor. When questioning the employer Fair Work Inspectors should use the Compliance Tool Notional Employer/Principal.

In some cases, the evidence does not clearly indicate the nature of the arrangement. In the first instance, a Fair Work Inspector should review the case with their team leader, manager or principal investigator to decide whether an assessment can be made, whether further evidence can be acquired, or if legal advice is required.

It is critical that any assessment made in relation to status of employment is fully documented, including the evidence upon which it was based. If the matter is litigated and the employer disputes the Fair Work Inspector’s assessment regarding the status of

employment, the court will be required to look at all the factors and determine whether the person is an employee or a contractor.

7.4.8 Assistance from Legal Group

Where the determination is difficult, the Fair Work Inspector should contact Legal Group for advice and assistance in making an assessment. Legal Group will provide advice as to the likely determination a court may make regarding the complainant's status of employment. To assist Legal Group the Fair Work Inspector must provide the allocated lawyer all available information relevant to the multi factor test.

7.4.9 Where the Fair Work Inspector assesses that the complainant is an employee

Where the Fair Work Inspector, having applied the multi factor test, finds that the complainant is an employee, but has been treated like a contractor, the Fair Work Inspector will need to investigate to determine whether the complainant has received their correct entitlements as an employee. (Consideration would also need to be given as to whether this was a sham contracting arrangement, as detailed in Chapter 20 – Termination and contractors).

7.4.10 Where the Fair Work Inspector assesses that the complainant is a contractor

In some circumstances, the Fair Work Inspector (having applied the [above tests](#)) will find that the complainant is an independent contractor and not an employee. If the complaint related to alleged underpayment of employee entitlements under the [FW Act](#), the Fair Work Inspector must advise the complainant that as they are not an employee, the entitlements sought under the FW Act do not apply.

The FWO does not have jurisdiction to investigate complaints made by independent contractors who allege that they have not been provided with the payments or conditions due under their contract for service, or who believe their contract is unfair or harsh. Such complainants will need to pursue their own action through the courts in this regard. Complainants seeking further advice may be referred to the Independent Contractors Hotline on 1300 667 850.

However, there may still be matters for FWO to investigate in relation to a contractor (e.g. if there are apparent or alleged freedom of association matters under the [FW Act](#) or prohibited conduct under the [IC Act](#)). In such cases, the Fair Work Inspector should further investigate these matters in accordance with their powers under the relevant legislation (refer Chapter 1 - Introduction ,section 1.3))

Where parties to an investigation require information related to the difference between employees and independent contractors, Fair Work Inspectors can refer them to the fact sheet '[Independent contractors and employees](#)'.

20.5 Sham contracting

A 'sham contract' is an arrangement where an employer attempts to disguise an employment relationship as an independent contracting arrangement, usually for the purposes of avoiding responsibility for employee entitlements.

Part 3-1, Division 2 of the [FW Act](#)¹ provides that it is a contravention to:

¹ FW Act; ss357-359. These provisions were introduced by the *Workplace Relations Legislation Amendment*

- misrepresent an employment relationship or a proposed employment relationship as an independent contracting arrangement
- dismiss or threaten to dismiss an individual for the purpose of engaging them as an independent contractor to perform the same role, or a role which is substantially the same work
- knowingly make a false statement to persuade or influence a person to enter into a contract for services in certain circumstances.

Fair Work Inspectors can seek the imposition of penalties for contraventions of the [FW Act](#) in relation to sham contracts. Fair Work Inspectors may also apply to the court to grant an injunction in a situation where an employer dismisses or threatens to dismiss an employee for the purpose of re-engaging the employee as an independent contractor (refer Chapter 23 – Enforcement, section 23.7 - Injunctions).

20.5.1 Investigating alleged sham contracts

20.5.1.1 Is the worker an employee?

When investigating allegations of sham contracting, Fair Work Inspectors will generally be required to obtain evidence of both the ‘sham arrangement’ proposed or in place, and the legitimate employment relationship that was actually proposed or existed. Such evidence should be obtained from a variety of sources which may include (but are not limited to):

- record of conversations with the complainant(s)
- record of interview with the employer/principal
- witness statements from employees
- invoices issued by the complainant(s)
- correspondence between the parties
- timesheets, rosters, details of leave taken
- employer policies
- documents detailing payments made to the complainant(s) by the employer/principal
- offers, quotes or contracts entered into between the parties
- documents detailing payment arrangements between the parties
- induction or training forms
- ABN details for the complainant(s)
- Tax File Number Declaration forms
- job advertisements, sub-contractor tender notices
- certificates of currency of Workers Compensation insurance
- directions or instructions on work or performance
- legal advices and activities relevant to the defence
- ASIC company searches
- business name searches
- letter of termination; final payslip

This evidence is necessary to establish that the worker, who is being treated as an independent contractor, should properly be treated as an employee. Fair Work Inspectors will need to make use of the multi factor test [questionnaire](#) to establish whether an

employment relationship or contracting arrangement exists (refer to Chapter 7 – Wages and conditions investigations, section 7.4 – Confirming the employment or contractor status).

It is important to note that Fair Work Inspectors will also need to determine whether the complainant has received their correct entitlements as an employee. Where appropriate, Fair Work Inspectors may refer parties to an investigation to '[Independent contractors and employees](#)' fact sheet or the [FWO's website](#), which includes some information specific to the cleaning, contact centre and hair and beauty industries.

20.5.1.2 Assistance from Legal Group

In some cases, the evidence does not clearly indicate the nature of the arrangement. In the first instance, a Fair Work Inspector should review the case with their team leader, manager or principal investigator to decide whether an assessment can be made, whether further evidence can be acquired, or if legal advice is required.

It is critical that any assessment made in relation to status of employment is fully documented, including the evidence upon which it was based. If the matter is litigated and the employer/principal disputes the Fair Work Inspector's assessment regarding the status of employment, the court will be required to look at all the factors and determine whether the person is an employee or a contractor.

20.5.1.3 Where the Fair Work Inspector assesses the complainant is a contractor

In some circumstances, the Fair Work Inspector (having applied the above tests) will find that the complainant is an independent contractor and not an employee. If the complaint related to alleged underpayment of employee entitlements under the [FW Act](#), the Fair Work Inspector must advise the complainant that as they are not an employee, the entitlements sought under the FW Act do not apply.

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20.5.1.4 Where the Fair Work Inspector finds the employee is being treated as an independent contractor

Where the Fair Work Inspector, having analysed all the evidence and applied the multi factor test, finds that the complainant is an employee, but has been treated like a contractor; section 357(1) of the FW Act² has been established. Having found that, the employer

² A person that employs, or proposes to employ, an individual must not represent to the individual that the contract of employment under which the individual is, or would be, employed by the employer is a contract for services under which the individual performs, or would perform, work as an independent contractor.

contravened section 357(1) it is appropriate to consider whether the defence provided for in section 357(2) is likely to be available to the employer..

20.5.2 Statutory defence to alleged sham contracting

A statutory defence exists in relation to the [FW Act](#) (misrepresenting an actual or proposed employment relationship).³ The FW Act provides an employer will not have contravened these provisions if the employer proves that, at the time the alleged misrepresentation occurred, the employer did not know and was not reckless as to whether the contract would be a contract *of* employment rather than a contract *for* services (i.e. an independent contract arrangement).⁴

Accordingly, the Fair Work Inspector should attempt to investigate the employer's "actual belief" as to the nature of its relationship with the worker(s) and the circumstances of implementing the arrangements (i.e. whether legal advice was sought), so as to ascertain whether the misrepresentation was made knowingly or recklessly. Where the employer has received legal advice, Fair Work Inspectors can request this legal advice with an NTP.

Where possible, Fair Work Inspectors should interview company directors, managers and/or persons who have control of the employer entity. In this instance, any legal advice the employer was acting on may be relevant. As such, the employer may wish to waive legal professional privilege.

20.5.3 Enforcement methods

20.5.3.1 Sham Contracting

Where a Fair Work Inspector determines that the defence has not been made out, or is not considered a statutory defence in accordance with s357(2) of the FW Act, and thus the employer has engaged in sham contracting, the Fair Work Inspector should discuss the matter with their team leader and consider a relevant compliance mechanism, such as a contravention letter, enforceable undertaking or litigation. For further information on suitable enforcement methods, please refer to Chapter 23 – Enforcement.

20.5.3.2 Illegitimate contracting

If a Fair Work Inspector determines that the employer did not know; and was not reckless as to whether; the contract was one of employment (s357(2) of the FW Act), this does not mean the form of engagement is legitimate, rather the form of engagement can be described as "illegitimate contracting". The Fair Work Inspector is to issue a [special letter of caution](#) to bring about voluntary compliance. Importantly, the educative nature of this formal caution means the defence in section 357(2) of the FW Act will not be available to the employer in the future.

Fair Work Inspectors should note that in addition to issuing the letter of caution, the matter may need to be referred to the ATO, as there may be issues regarding tax and non payment of superannuation contributions. Fair Work Inspectors should discuss this with their team leader before referring matters.

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³ FW Act; s 357(1)

⁴ FW Act; s 357(2)