

EMPLOYEE OR INDEPENDENT CONTRACTOR: DON'T GET CAUGHT OUT!

Businesses that engage workers as an “independent contractor” when they are really an “employee” can face serious consequences.

A recent Board of Taxation review found that many workers were incorrectly claiming to be business entities to gain a tax advantage. There are 1 million contractors in Australia, and a Tax Office audit last year of 67 contractors found 84 per cent breached tax rules.



The distinction between who is a contractor and who is an employee can be a grey area at times, however it is important that the right distinction is made as different legal and tax obligations apply.

Even if someone quotes an ABN and provides a tax invoice with GST charged you may still have an obligation to meet award obligations, deduct PAYG tax, pay payroll tax, pay 9.5% super and/or declare their payment under your WorkCover policy.

The following information provides an outline to help you determine whether your workers are in fact contractors or employees.

This is only a guide and we recommend clients with concerns about this issue contact us to discuss your particular circumstances.

How do you determine the difference?

There are a number of factors to consider in determining whether a worker is an employee or an independent contractor and you must examine all the details in each case.

According to the ATO, a key factor in deciding if a worker is an employee is the degree of control that can be exercised over the worker. If the payer has the right to direct how, when, where and who is to perform the work, the worker is likely to be an employee. These directions may be verbal or in writing, or simply understood between the parties.

Past Tax Office rulings have placed considerable weight on the relationship between the worker and the payer – whether it is seen as a contract OF service (a master-servant type relationship) or a contract FOR service (freedom for the contractor to work unsupervised to achieve an end result). Consider whether the worker is being paid for the time they work, or being paid for a result. It's not always clear cut, but workers being paid by the hour are more likely to be employees while workers being paid for a result are more likely to be contractors.

INFORMATION IN THIS FACT SHEET HAS BEEN
SOURCED FROM THE ATO.

THIS FACTSHEET IS GENERAL IN NATURE, PLEASE
CONTACT BMO 4662 3722 TO SEEK ADVICE
PARTICULAR TO YOUR INDIVIDUAL
CIRCUMSTANCES.

So what's an "Employee"?

Generally, a worker is an employee if they:

- ▶ are paid for time worked
- ▶ receive paid leave (for example, sick, annual or recreation, or long service leave)
- ▶ are not responsible for providing the materials or equipment required to do their job
- ▶ must perform the duties of their position
- ▶ agree to provide their personal services
- ▶ work hours set by an agreement or award
- ▶ are recognised as part and parcel of the payer's business, and
- ▶ take no commercial risks and cannot make a profit or loss from the work performed.

If a worker is an employee, the payer must withhold an amount from any salary, wages, commissions, bonuses or allowances they pay to the employee. The payer determines the amount to withhold using the tax tables published by the Tax Office.

An employer may also have obligations under fringe benefits tax, payroll tax, WorkCover, and the superannuation guarantee laws.

What's an "Independent contractor"?

An independent contractor is an entity (such as an individual, partnership, trust or company) that agrees to produce a designated result for an agreed price. In most cases an independent contractor:

- ▶ is paid for results achieved
- ▶ provides all or most of the necessary materials and equipment to complete the work
- ▶ is free to delegate work to other entities
- ▶ has freedom in the way the work is done
- ▶ provides services to the general public and other businesses
- ▶ is free to accept or refuse work, and
- ▶ is in a position to make a profit or loss.

Even if the worker is deemed an "independent contractor", you may still be liable to pay the 9.5% super guarantee payments, especially if it is a contract job principally for labour only. WorkCover obligations may also apply in these circumstances.

Contractor vs Employee – A guide:

Control over work - The employee works under the direction and control of an employer.

A contractor is free to exercise their own discretion. (A payer has a right to specify how the contracted services are to be performed, but this must be specified in the terms of the contract).

Independence - An employee performs work for the employer in accordance with an employment contract.

A contractor performs services as specified in a contract with the payer and provides additional services only by agreement.

Payment - Payment is often based on the period of time worked, but an employee can also work on 'piece rates' or commission.

For a contractor, payment is dependent on the performance of the contract services.

Commercial risks - An employee generally bears no legal risks in respect of the work; since the employee works in the business of the employer, the employer is legally responsible for any work performed by the employee.

A contractor bears legal risk in respect of the work. They have the potential to make a profit or loss, and must remedy any defective work at their own expense.

Ability to delegate - An employee performs the work personally and generally cannot subcontract the work to someone else.

Unless otherwise specified in the contract, a contractor can subcontract or delegate the work.

Tools and equipment -

The employer usually provides tools and equipment.

Generally, a contractor provides their own tools and equipment. To be deemed a contractor, this would need to be substantial equipment – not just hand tools.