

Employment, Workplace Relations & Safety

Update: ABCC issues Discussion Paper on sham contracting arrangements

The ABCC has commenced an Inquiry into the use of sham contracting and the use of labour hire in the building and construction industry by issuing a Discussion Paper, followed by a series of national Roundtable conferences, with a view to developing a Code of Practice for the industry.

WHAT HAS HAPPENED?

- In December 2010, the Australian Building and Construction Commission (**ABCC**) published a Discussion Paper as part of its Inquiry into the use of sham contracting and the use of labour hire in the building and construction industry (**Discussion Paper**). Submissions on the Discussion Paper are due by 7 March 2011, and must be submitted through an online submission process at www.abcc.gov.au/shamcontracting.
- The ABCC will be holding national Roundtable conferences about the Discussion Paper with key stakeholders, such as Federal and State Ministers, regulatory agencies, unions and employer organisations in late March/early April 2011.
- Participation in the Inquiry is voluntary. However, any material that comes out of the Roundtable conferences, or the responses to the Discussion Paper, will be public information (unless otherwise agreed with the Commissioner), and may trigger an investigation by the ABCC, or be used as evidence in civil penalty litigation.
- As a result of the Inquiry, the Commissioner may, for the first time, develop a Code of Practice for Labour Hire in the building and construction industry. If issued by the Minister using his power to do so under the *Building and Construction Industry Improvement Act 2006 (Cth)*, the Code would have the status of a legislative instrument, and therefore allow the

Commissioner to direct a person to provide a written report about the extent to which they have complied with the Code. Failure to comply with that direction may result in a fine of around \$11,000.

- The ABCC shares jurisdiction with the Fair Work Ombudsman (**FWO**) for enforcement of the sham contracting and underpayment provisions of the *Fair Work Act 2009 (Cth)* (**FW Act**). The ABCC has agreed with FWO that from 1 March 2011, all building industry underpayment matters will be pursued by the ABCC.
- Employers may also expect more audits by the Australian Tax Office. The ATO issued a statement in June 2010 that it would be focussing on sham contracting arrangements, and visiting high risk businesses (including construction) in all capital cities and regional areas to review their employment and contracting arrangements.

SHAM CONTRACTING AT A GLANCE

'Sham contracting' is where an employer attempts to disguise an employment relationship as an independent contracting relationship or consultancy. Specifically, the FW Act already prohibits the following:

- **Misrepresentation of genuine employment:** misrepresenting an employment arrangement, or a proposed employment arrangement, to be an independent contracting arrangement (s.357);

- **Re-engagement:** dismissing or threatening to dismiss a current employee in order to engage them as an independent contractor to perform the same or substantially the same work (s.358); or
- **False and misleading statements:** making a knowingly false statement to an employee or former employee in an attempt to persuade the individual to enter into a contract for services (s 359).

Each of these provisions is a civil penalty provision, entailing a current maximum penalty of \$6,600 for an individual and \$33,000 for a company. A court also has the power to make other orders, such as making an award of damages for loss (eg. underpayment under an applicable award or enterprise agreement), granting an injunction or ordering reinstatement.

The Independent Contractors Act 2006 (Cth) (IC Act) also provides an avenue for contractors to challenge unfair terms of their contracts. Although the IC Act does not specifically prohibit sham contracting, it does provide a disincentive for entering into a sham arrangement as it provides potential remedies in relation to an unfair contract even if the worker cannot establish that they are an employee. In determining if a contract is unfair, the Court may take into account how the remuneration received compares with the wages a comparable employee would have received (under an award or industrial instrument) and may make an order for recovery of additional payment.

Both the FW Act and the IC Act rely on the common law definitions of “employee” and “contractor”. The courts have developed a multi-factor test to determine whether a worker is an employee or a contractor. The test looks at the totality of the relationship between the parties, including issues such as how much control the principal exercises over the worker, who provides equipment, how the worker is paid and whether the worker has the right to work for third parties.

The ABC Commissioner, Leigh Johns, has indicated that he may recommend changes to the FW Act and IC Act as a result of the Inquiry.

WHY HAS THE ABCC COMMENCED THIS INQUIRY?

In announcing the Inquiry into sham contracting arrangements on 19 November 2010, the ABC Commissioner Leigh Johns said that the Inquiry and the Roundtable are a fundamental component of his

vision for the role of the ABCC as it moves to becoming a full service regulator. The ABCC is already taking a more active role in prosecution of sham contracting, which it has historically referred to FWO. As at December 2010, ABCC has one matter before the Federal Magistrates Court in Sydney, with a further dozen or more cases under investigation which may proceed to litigation.

Commissioner Johns identified several shortcomings of the present regulation of sham contracting, including:

- the sham contracting provisions under the FW Act (and the equivalent provisions under the former *Workplace Relations Act 1996 (Cth)* have been rarely utilised;
- civil penalty litigation under those provisions is unlikely on its own to generate significant change in the industry, partly because the common law test of who is an employee is complex and difficult to apply, and each case will turn on its own facts; and
- many potential complainants are reluctant to report breaches to the ABCC for fear of triggering an investigation into their own taxation and business arrangements

For these reasons, the ABCC needs to consider alternative ways in which sham contracting arrangements and the use of labour hire in the construction industry generally can be effectively dealt with.

THE DISCUSSION PAPER - AN OVERVIEW

The matters covered by the Discussion Paper are framed by the Terms of Reference:

- Sham contracting provisions under sections 357 to 359 of the FW Act;
- Employees, independent contractors, subcontracting and working arrangements in the building industry;
- The role of labour hire companies in the building industry;
- The current definitions of “employee” and “independent contractor” at common law and in statutes;
- The evasion by employers of responsibilities owed to employees in the building industry by

use of devices including subcontracting and labour hire arrangements;

- The evasion by workers in the building industry of taxation and other responsibilities by use of devices including creating businesses and partnerships;
 - Competitions and “undercutting” in the building industry: the role played by labour hire companies and subcontractors; and
 - Fairness: inequality of bargaining power as a driver in contractual negotiations between employers and workers.
- Interested parties can make contributions and access resources related to the Inquiry at <http://www.shamcontractinginquiry.gov.au>.
 - Employers should consult with legal advisers in the preparation of any response if there is a risk that there are any potential grounds for an investigation of them by the ABCC.
 - Employers should audit their own contracting arrangements, both with contractors directly and with labour hire companies, to see if any changes need to be made to avoid potential prosecutions given the likelihood of an increased focus on these issues.
 - Employers should train managers involved in recruitment as to the differences between employees and contractors and the sham contracting provisions of the FW Act, to minimise the risk of being found to be in breach of the FW Act.

For each topic, the Discussion Paper poses a series of questions to which responses are invited. Respondents are also invited to address the adequacy of the Terms of Reference if they consider that additional areas should be covered.

WHAT DOES THIS MEAN FOR EMPLOYERS?

- Given the likely outcome of the Inquiry will be the formulation of a Code of Practice in this area, employers should consider participating in the Inquiry, including preparing a response to

This article was produced by Herbert Geer.
It is intended to provide general information in summary form on legal issues.
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