WEstjustice

21 December 2018

Black Economy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: Blackeconomy@treasury.gov.au

Dear Black Economy Division

WEstjustice response to questions set out in the *Improving Black Economy Enforcement and Offences Consultation Paper*

WEstjustice welcomes the opportunity to submit this response to the questions set out in the *Improving Black Economy Enforcement and Offences Consultation Paper* (**Consultation Paper**) prepared by the Treasury of the Australian Government. We would also welcome the opportunity to discuss our views and recommendations as part of the ongoing consultation process.

We congratulate the Government on taking this initiative to address the harms caused by the black economy, including its focus on reducing sham contracting. We urgently need to reform our legal frameworks and enforcement processes with respect to sham contracting.

This submission seeks to address two questions, set out in Part 3.7 of the Consultation Paper, which are most relevant to the WEstjustice Employment Law Program, specifically:

- Question 14: What level of increase to the civil penalties would serve as an appropriate deterrent to stop employers from engaging in sham contracting arrangements?

- Question 15: Is the existing 'reckless' threshold for prosecuting employers involved in sham contracting appropriate? Should this legal threshold be lowered to a 'reasonableness' test?

Summary of recommendations

In this submission, we make **four recommendations:**

1. Contravention of the sham contracting provisions not only constitutes a grave contravention of the *Fair Work Act 2009* (Cth) (**FW Act**) but also undermines the workplace relations framework by providing non-compliant companies with an unlawful competitive advantage. The gravity and anti-competitive nature of the contraventions should be reflected in the maximum penalties which a court may impose.

2. The existing 'reckless' threshold for prosecuting employers involved in sham contracting is ineffective. The FW Act should be amended to include a statutory definition of employee. It should include a presumption that a worker is an employee.

   To remove the perverse incentive to engage in sham contracting, the law must be amended to provide all workers with the right to the minimum pay and entitlements, unless the employer/principal can show that the worker was genuinely running their own business. In addition, more rigorous tests should be applied before an ABN is given to an individual. On the

spot ABN inspection and assessment should also be increased.

3. Employers and principals should have a positive obligation to ensure they classify their workers appropriately. There should be no recklessness/lack of knowledge defence. Accordingly, we recommend that section 357(2) of the FW Act be repealed.

4. In the alternative to Recommendations 2 and 3, we support recommendation 10.3 of the *Black Economy Taskforce Final Report* (**Taskforce's Report**). Specifically, if section 357(2) of the FW Act is to be retained, we support lowering the legal threshold under s 357 of the FW Act to a 'reasonableness' test.

Our proposals are set out in further detail below.

About WEstjustice and the Employment Law Program

WEstjustice is a community organisation that provides free legal help to people in the western suburbs of Melbourne. Our offices are located in Footscray, Werribee and Sunshine, with a number of outreach services.

We assist with a range of everyday legal problems including consumer disputes, credit and debt, family law and family violence, fines, motor vehicle accidents, tenancy, and employment related matters.

We also provide free community legal education, undertake law reform activities and work in partnership with local communities to deliver innovative projects that build legal capacity and improve access to justice.

With a long history of working with migrant and refugee communities, in 2014 we identified a large unmet need for employment law assistance for these communities, who are particularly vulnerable to exploitation at work. In response, WEstjustice established the Employment Law Project, which provided legal assistance to over 200 migrant workers from 30 different countries, successfully recovering or obtaining orders for over $120 000 in unpaid entitlements and over $125 000 in compensation for unlawful termination. We also trained over 600 migrant workers, as well as leaders from migrant communities and professionals supporting these communities. Based on evidence from our work, and extensive research and consultation, WEstjustice released the Not Just Work Report,[1] outlining 10 key steps to stop the exploitation of migrant workers.

Given continuing and unmet need, WEstjustice now operates an ongoing Employment Law Program. The Program seeks to improve employment outcomes for vulnerable workers including migrants, refugees and temporary visa holders. We do this by empowering migrant and refugee communities to understand enforce their workplace rights through the provision of tailored legal services, education, sector capacity building and advocacy for systemic reform. To date our service has recovered over $400 000 in unpaid entitlements or compensation, trained over 1000 community members, delivered four roll-outs of our award-winning Train the Trainer program, and participated in numerous law-reform inquiries and campaigns.

WEstjustice Legal Service: Sham contracting

WEstjustice has provided significant casework support to workers who have experienced sham contracting. In its first 16 months of operation, around 8% of Employment Law Project legal service clients received advice on sham contracting. This was concentrated in particular industries, including the construction industry, where around half of our clients received advice in relation to sham

[1] Catherine Hemingway, *Not Just Work: Ending the exploitation of refugee and migrant workers* (2016): https://www.westjustice.org.au/cms_uploads/docs/westjustice-not-just-work-report-part-1.pdf.

contracting. In a sample of 35 cleaning clients from the past four years, we found that 31% received advice in relation to sham contracting.

Sumit's story provides a powerful example of the challenges our client's face in detecting and enforcing breaches of the law:

SUMIT

Sumit cannot read or write in his own language, or in English. He worked as a cleaner and was engaged in a sham contracting arrangement. Sumit had never heard of the difference between contractors and employees, nor was he aware of the minimum wage. We assisted Sumit to calculate his underpayment and write a letter of demand to his former employer. Sumit could not have done this without assistance, and no government agencies can help with these tasks. Sumit's employer did not respond, so we assisted him to complain to FWO. The employer did not attend mediation, and FWO advised Sumit that the next step would be a claim in the Federal Circuit Court - however they could not assist him to complete the relevant forms. There is no agency to assist Sumit write this application and he could not write it without. help. WEstjustice helped Sumit to write the application.

Our submission contains case studies and evidence-based recommendations for reform. All of the case studies in this submission are based on the experiences of our clients.[2]

Question 14: What level of increase to the civil penalties would serve as an appropriate deterrent to stop employers from engaging in sham contracting arrangements?

RECOMMENDATION 1

Contravention of the sham contracting provisions not only constitutes a grave contravention of the *Fair Work Act 2009* (Cth) (**FW Act**) but also undermines the workplace relations framework by providing non-compliant companies with an unlawful competitive advantage. The gravity and anti-competitive nature of the contraventions should be reflected in the maximum penalties which a court may impose.

Question 15: Is the existing 'reckless' threshold for prosecuting employers involved in sham contracting appropriate? Should this legal threshold be lowered to a 'reasonableness' test?

"The only legal risk facing an employer who misclassifies a worker is the risk that it may ultimately be required to shoulder an obligation it thought it had escaped."[3]

Under Australian law, employees are treated very differently to independent contractors. Employees are afforded various protections under the FW Act including the right to a minimum wage, maximum hours of work, leave entitlements and protections from unfair dismissal.

With the exception of limited protections (for example, some general protections provisions and anti-discrimination laws), independent contractors are largely excluded from the protections of the workplace relations framework. Under the FW Act, it is unlawful to engage a worker as a contractor when they are in reality an employee (sham contracting). To determine whether a worker is running their own business (as a contractor), or in fact an employee, courts apply a multi-factor common law test. Considerations include whether the worker was required to wear a uniform, provided their own tools and equipment, was paid an hourly rate or paid to complete a task, could delegate work or was required to complete work personally, and the degree of control the employer exercised over the worker (e.g. hours of work, manner of work etc).

[2] Note that names have been changed in these case studies.

[3] Joellen Riley, 'Regulatory responses to the blurring boundary between employment and self-employment: a view from the Antipodes' (Recent Developments in Labour Law, Akademiai Kiado Rt, 2013), 5.

The nature of any agreement/contract between the worker and boss is not determinative (that is, a written contract stating that an individual is an independent contractor does not necessarily mean they will be considered or classified as such at law).

Among newly arrived and refugee communities, sham contracting is rife. In a WEstjustice survey, the following comments were provided by community workers who were asked a general question about common employment problems:[4]

"Client was told they would only hire him if he had an ABN."

"Clients don't know their rights and what they should be paid. They are taking jobs and using ABNs without knowing what that means."

"A lot of clients are told by employers they have to obtain ABNs even though it's not appropriate for the work they are doing."

In our experience at the ELS, sham contracting is used systematically as a core business practice throughout the road transport and distribution services, the cleaning industry, the home and commercial maintenance industries (e.g. painters), and in the building and construction industry (e.g. tilers). WEstjustice has witnessed numerous clients working in these industries whose employment relationship was actually one of employer-employee. Clients were paid an hourly /daily rate, wore a uniform, had all equipment provided by the employer, worked for only one employer, were unable to take time off work and were unable to subcontract. We have also assisted clients in sham contracting arrangements outside of these key industries, including in the education and administration sectors.

WEstjustice has observed instances of employers obtaining ABNs for workers, and instances of jobs being offered, conditional upon having an ABN. There is often little if any choice in a worker's 'acceptance' of their position as a contractor. Often that type of engagement is the only one on offer and is made on a 'take it or leave it' basis.

For someone desperate to make a start in a new country, the basic need to work and earn an income is often overshadowed by the terms and conditions under which the work is offered. This creates a power imbalance, and in many instances, principals take advantage of the vulnerability of potential workers in this situation.

We have observed that sham contracting can take place through complex sub-contracting and supply chain arrangements with multiple intermediaries between the original employer and the 'independent contractor'. It is an issue that disproportionately affects individuals with limited agency in the labour market. Some of our clients' experiences are set out in the following case studies.

LIN

Lin came to Australia as a refugee. This was her first job in Australia. She worked as a door-to-door sales person trying to sell safety equipment. She was given instructions on where to work, how and when. The boss agreed to pay $60 per sale but no salary apart from this. After three full days of work (8am–5pm) Lin left her job.

She had made one sale but was never paid for it despite providing her ABN and bank details. Lin came to see us about the $60 payment, without any understanding of the differences between an independent contractor and employee, or the right to be paid an hourly wage.

[4] Full details can be found at Catherine Dow, *Employment is the Heart of Successful Settlement* (2014): http://www.westjustice.org.au/cms_uploads/docs/westjustice-employment-is-the-heart-of-successful-settlement-report.pdf, 12.

BAO

Bao worked as an independent contractor delivery driver for a distribution company. He worked full time making deliveries for one host agency. He wore their uniform, was texted each night confirming work the next day, and had no control over hours or duties. Bao had a contract providing for subcontracting but in reality he was not able to delegate. He was paid by the hour and was not allowed to take days off, even with a medical certificate. Bao's boss kept several weeks pay 'in advance'. Bao was told if he went home (overseas) to visit his family he he would not be paid and would not get future shifts.

CAMILA

Camila came to Australia from South America on a student visa. She worked as a cleaner for Diego and was asked to provide him with invoices at the end of each month in order to be paid. Camila was often paid late, or not at all for her work.

Camila came for assistance as she did not receive payment for an invoice from Diego. WEstjustice advised Camila that she may be engaged in a sham contract and explained to her the difference between an employee and a contractor. The lawyer further advised Camila about her entitlements as an employee and that her underpayments claim could be much more significant than the unpaid invoice. Camila asked WEstjustice to calculate her entitlements as an employee. In the meantime, Diego paid Camila for the outstanding invoice.

Through this process Camila became more aware of her rights, and so with WEstjustice's help, Camila made a complaint to the FWO to ensure that Diego will not exploit other workers in the same way she was.

Sham contracting results in exploitation

The problems our clients face as a result of being falsely engaged as an independent contractor when in fact they are employees include:

- they do not receive minimum award wages or entitlements, including leave. Our clients are mostly people who are low paid, award-reliant workers doing unskilled or low-skilled labour. They are performing the work of an employee, which should entitle them to the same rights and standards enjoyed by employees under the FW Act. Individuals who are ostensibly employees are therefore receiving less than their position ought to afford them. This creates serious issues for the labour market in terms of providing a competitive advantage to those companies that misclassify and underpay their workers;

- they rarely receive superannuation contributions. This is the case even though Superannuation Guarantee Ruling 2005/1 provides that they must receive superannuation contributions if they are engaged under a contract that is principally for labour.[5] A contract will be principally for labour if it is mainly for the person's labour, which may include:

    - physical labour;

    - mental effort; or

    - artistic effort;

[5] Australian Taxation Office, *Superannuation guarantee: who is an employee?,* SGR 2005/1, 23 February 2005.

- contractors are often required to arrange their own tax and may need to organise workers compensation insurance, however many vulnerable contractors are not aware of how to do this.

Many of our clients are not aware that there is a difference between an employee and independent contractor, and asking the questions necessary to apply the multi-indicia test can be difficult. It is a cause for grave concern that our clients are often told by the person hiring them that if they have an ABN they are automatically a contractor, or told they will not be paid unless they obtain an ABN.

In many circumstances we find that in reality it is exceedingly difficult to resolve the initial problem of correctly identifying a worker as an employee. Applying the multi-factor test and attempting to convince an employer that their characterisation of their worker is incorrect is both a time and resource-intensive task. Many of our clients are so desperate for payment that they often opt to accept their misclassification as an independent contractor and seek to enforce the non-payment of their contractor agreement in the relevant tribunal or court. The client is then left to 'accept' what would otherwise be an underpayment claim and a loss of accrued entitlements such as annual leave. They may also forfeit their ability to bring other claims for unfair dismissal. Reform is urgently required.

Amendment of the FW Act is required

"Except perhaps in matters involving revenue authorities, a rational if unethical employer may consider it worth classifying a worker as a contractor, because the employer might make immediate savings and face only a remote risk that the employee would ultimately find reason to bring a grievance."[6]

Removing legislative incentives to rip off vulnerable workers is a simple and cost-effective way to reduce exploitation. We recommend that rather than applying the multi-factor test to each situation where there is doubt as to a worker's true status, a statutory presumption would increase efficiency and certainty. This definition should assume that all workers are employees, unless proven otherwise. Importantly, our proposed amendment shifts the onus off vulnerable workers and onto an employer/principal to establish a genuine contracting relationship.

In their Submission to the ABCC Inquiry into Sham Arrangements and the Use of Labour Hire in the Building and Construction Industry, Andrew Stewart and Cameron Roles proposed that the term 'employee' should be redefined in a way that would strictly limit independent contractor status to apply only to those workers who are genuinely running their own business:[7]

'A person (the worker) who contracts to work for another is to be presumed to do so as an employee, unless it can be shown that the other party is a client or customer of a business genuinely carried on by the worker.'[8]

They recommend that this definition could be included in any legislation which uses the term 'employee'. WEstjustice supports this recommendation: the definition is precise and clear, and allows scope for genuine contractors to engage as such.

Building on this definition, WEstjustice proposes the following amendments to the FW Act:

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[6] Joellen Riley, 'Regulatory responses to the blurring boundary between employment and self-employment: a view from the Antipodes' (Recent Developments in Labour Law, Akademiai Kiado Rt, 2013), 5.

[7] Andrew Stewart and Cameron Roles, Submission to the Australian Building and Construction Commissioner (ABCC), <http://fwbc.gov.au/sites/default/files/Andrew%20Stewart%20and%20Cameron%20 Roles%20-%20SCRT%20Submission.docx>.

[8] Ibid. See also, Cameron Roles and Andrew Stewart, 'The reach of labour regulation: Tackling sham contracting' (2012) Australian Journal of Labour Law 25, 258.

Table 1: Sham contracting drafting suggetions		
Type of change	**Section**	**WEstjustice's drafting suggestions**
Amend existing provision	357	**357 Misrepresenting employment as independent contracting arrangement** (1) A person (the ***employer***) 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. Note: This subsection is a civil remedy provision (see Part 4-1). (2) Subsection (1) does not apply if the employer proves that, when the representation was made, the employer: (a) did not know; ~~and~~ (b) was not reckless as to whether; <u>and</u> <u>(c) could not reasonably be expected to know that</u> the contract was a contract of employment rather than a contract for services.
Insert new provision	357A	(1) <u>Regardless of whether an individual is engaged and treated as an employee under a contract of service or an independent contractor under a contract for services, that individual is taken to be an employee (within the ordinary meaning of that expression) for the purposes of this Act.</u> (2) <u>Subsection (1) does not apply if it can be established that the individual was completing work for a client or customer of a business genuinely carried on by the individual.</u>

Alternatively, the ATO's superannuation eligibility test could be adopted more broadly. That is, if a worker is engaged under a contract wholly or principally for the person's physical labour, mental effort, or artistic effort, that person should be deemed to be an employee for all purposes.[9]

A definition similar to those outlined above would assist our clients to enforce their rights more efficiently, without inhibiting the ability of those who are genuinely independent to contract accordingly.

Currently, in order for an individual to receive compensation for underpayment as a result of sham contracting, an individual must make a claim in the appropriate jurisdiction (the Federal Circuit Court or Federal Court of Australia) establishing:

- that they were an employee; and
- their appropriate award classification, rate of pay and underpayment.

It is unrealistic to expect that newly arrived and refugee workers will be able to prepare a claim that requires knowledge of a common law 'multi-factor' test. There is also a risk that if the complex multi-factor test is applied differently by the Court and workers are not found to be employees, they would have been better off making an application to VCAT as an independent contractor.

[9] Australian Taxation Office, Superannuation guarantee: who is an employee?, SGR 2005/1, 23 February 2005.

Unfortunately, the complex multi-factor test is preventing workers from pursuing their full entitlements. A statutory definition that presumes workers are employees affords many advantages: less time is used in applying a vague multi-factor test, there is greater likelihood of consistent outcomes, increased clarity for employers and employees, and there is much greater fairness for workers.

RECOMMENDATION 2

The existing 'reckless' threshold for prosecuting employers involved in sham contracting is ineffective. The FW Act should be amended to include a statutory definition of employee. It should include a presumption that a worker is an employee. To remove the perverse incentive to engage in sham contracting, the law must be amended to provide all workers with the right to the minimum pay and entitlements, unless the employer/principal can show that the worker was genuinely running their own business (see proposed drafting in **Table 1**.

In addition, more rigorous tests should be applied before an ABN is given to an individual. On the spot ABN inspection and assessment should also be increased.

Employer defence should be limited

WEstjustice regards the current provisions in the FW Act as insufficient to discourage sham contracting. The provisions of subsection 357(2) should be dramatically re-written. The subsection provides:

> (2) Subsection (1) does not apply if the employer proves that, when the representation was made, the employer:
>
> a. did not know; and
>
> b. was not reckless as to whether;
>
> the contract was a contract of employment rather than a contract for services.

The provision offers a defence to an employer which is broad and relatively easy to rely upon.

Employers are in a far superior position to a worker in terms of resources and knowledge of the workplace relations system. They should have a duty to undertake the necessary consideration and assessment of whether or not a worker is an employee or independent contractor. They should be able to positively assert that the relationship they are entering into with a worker is the correct one.

As such, WEstjustice supports Productivity Commission recommendation 25.1 that:[10]

> The Australian Government should amend the FW Act to make it unlawful to misrepresent an employment relationship or a proposed employment arrangement as an independent contracting arrangement (under s. 357) where the employer could be reasonably expected to know otherwise.

Proposed drafting is set out in **Table 1**.

[10] Productivity Commission, Workplace Relations Framework, Inquiry Report No 76 Volume 2 (30 November 2015), http://www.pc.gov.au/inquiries/completed/workplace-relations/report/workplace-relations-volume2.pdf , 815.

RECOMMENDATIONS 3 AND 4

Employers and principals should have a positive obligation to ensure they classify their workers appropriately. There should be no recklessness/lack of knowledge defence. Accordingly, we recommend that section 357(2) of the FW Act be repealed.

In the alternative, we support recommendation 10.3 of the Taskforce's Report. Specifically, if section 357(2) of the FW Act is to be retained, we support lowering the legal threshold under s 357 of the FW Act to a 'reasonableness' test.

We would be pleased to discuss any aspect of our submissions further.

Thank you for allowing WEstjustice the opportunity to make this submission.

Yours sincerely,

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