Another contractor prosecuted by Fair Work for “sham contracting” …How to avoid being the next explained

The Federal Circuit Court has held that an employer contravened two provisions of the *Fair Work Act* when it tried to dismiss an employee and then immediately re-engaged her as a contractor.

**The Facts**

The employer was a building contractor, and the employee worked for them as an excavator operator. The director of the company gave the employee a letter explaining that they could no longer employ her as an employee, but “would like to continue to utilise your labour, however, it would have to be on a sub-contractor basis, working on an ABN”.

When the employee rejected this proposal, she was dismissed with one day’s notice.

The court found that the employer had breached the *Fair Work Act*, which prohibits dismissing an employee in order to re-hire them as a contractor. It also found that the employee was entitled to a week’s notice rather than just one day. Despite his protests, the company’s owner and director was also found to have contravened both provisions as he was “involved in” the breaches.

The penalties have yet to be determined, but the four proven contraventions could attract a total penalty of more than $120,000.00.
Implications for employers

It is important for all employers to bear in mind that the law specifically prevents them from dismissing an employee in order to set up a “sham contracting” situation. Employers who attempt to create these arrangements can face investigation and heavy penalties, not only as a result of breaching the Fair Work Act, but also as a result of so-called “contractors” being later declared to be “workers” by the ATO or workers’ compensation bodies.

That in turn can lead to substantial payments to the ATO and the workers’ compensation body and more hefty fines and penalties.

How to avoid sham contracting

Rule 1. The case referred to in this article clearly shows rule 1. Don’t try to convert existing employees into contractors who will keep working just for you as before.

Rule 2. Don’t be conned by people who tell you they have a great system you can use to turn your employees into contractors without being caught for sham contracting. There is at least one organization promoting such a scheme which says it has been approved by the High Court. It is true that the organization was in a High Court case about their scheme….but they lost!

Rule 3. Take some time to learn the difference between a real contractor and an employee. Here is an extract from the website of the Fair Work Commission which is an excellent place to start:-

A. There are a number of factors which may contribute to determining the difference between an employee and an independent contractor. However, it is important to note that no single indicator can determine if a person is a contractor or an employee. Each determination is based on the individual merits of the work arrangement in place. Courts always look at the totality of the relationship between the parties when determining the status of a person’s employment.

B. There are some common indicators that may contribute to determining whether a person is an employee or independent contractor:

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<thead>
<tr>
<th>Indicator</th>
<th>Employee</th>
<th>Independent Contractor</th>
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<tbody>
<tr>
<td>Degree of control over work performed</td>
<td>Performs work under the direction and control of their employer, on an ongoing basis.</td>
<td>Has a high level of control in how the work is done.</td>
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<tr>
<td>Hours of work</td>
<td>Generally works standard or set hours (note: a casual employee’s hours may vary from week to week).</td>
<td>Under agreement, decides what hours to work to complete the specific task.</td>
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<tr>
<td>Expectation of work</td>
<td>Usually has an ongoing expectation of work (note: some employees may be engaged for a specific task or specific period).</td>
<td>Usually engaged for a specific task.</td>
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<tr>
<td>Risk</td>
<td>Bears no financial risk (this is the responsibility of their employer).</td>
<td>Bears the risk for making a profit or loss on each task. Usually bears responsibility and liability for poor work or injury sustained while performing the task. As such, contractors generally have their own insurance policy.</td>
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</table>
Rule 4. You should reduce the risks of you being caught for sham contracting by making sure you have proper contracts prepared by a lawyer with all your workers, whether they are employees or contractors.

Rule 5. If you are in concerns that what you are doing might be exposing you to risk of prosecution or need help with contracts for your workers, don’t ignore the issue but call the Employment law and Industrial Relations Team at McKays for help.

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