



Guide

Independent Contractor or Employee?

Business Broking and Real Estate Professionals

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Key Points?

- Whether a worker is classified as an independent contractor or employee will depend on all the circumstances of the relationship, not just one or two factors.
- Employers should be careful when engaging workers as contractors when in fact they should be employees - this may breach the “sham contracting” laws under the Fair Work Act.
- Employees can be engaged on a commission-only basis under the Fair Work Act, but they need to meet the Minimum Income Threshold Test and other important conditions.

Introduction

Business Brokers are typically engaged as contractors to a business. However, just because a worker is engaged as a contractor does not mean that they will be treated by law as one. Regardless of the form of the agreement, if the contractor has the characteristics of an employee, then the law may categorise that worker as an employee. Each case will depend on its own facts, so the Courts will always look at the totality of the circumstances to determine if a worker is a contractor or employee.

Contractor versus Employee?

The relationship between an employer and an employee is contractual, referred to as a “contract of service”. In contrast, an independent contractor is usually hired to do a defined task under a contract referred to as a “contract for services”. Typically, a contractor is independent of the employer and has no provisions for annual leave, sick leave or other statutory entitlements that an employee would have under the *Fair Work Act 2009*.

Whilst there are a number of factors that may help ascertain the difference between an employee and contractor, it's important to note that no single indicator can determine if a person is a contractor or employee. Courts will always look at all the circumstances of the relationship when determining the status of a person's employment.

There are some common indicators to assist in determining the difference:

- **Control:** where an employer exercises or has a right to exercise a high degree of control over a worker, it is likely that the worker will be regarded as an employee. Usually a contractor will be more autonomous whereas an employee performs work under the direction and control of their employer. Control can extend to when and where the work is performed, designation of the actual work to be performed and the manner in which the work is to be carried out.
- **Integration:** how a worker is integrated into the company's business. If the worker runs a business that is separate to that of the company, then it is more likely that the worker is an independent contractor. If the worker provides services through a corporate entity, that is more likely to be a contractor than a worker who is engaged as an individual.
- **Risk:** employees bear no financial risk (i.e. it is the employer's responsibility) whereas contractors bear the risk for making a profit or loss on each task and usually bear responsibility for poor work or job injuries (that is why contractors have their own insurance).
- **Hours:** employees generally work to standard or set hours, whereas a contractor will decide what hours to work in order to complete the specified task.
- **Pay:** employees are paid regularly (e.g. weekly, fortnightly or monthly) whereas contractor have an ABN and submit tax invoices for work completed or are paid at the end of the contract or project. Employees have income tax deducted by their employer whilst contractors pay their own tax and GST to the Australian Taxation Office.
- **Leave:** contractors do not receive paid leave, but employees are entitled to paid leave (e.g. annual leave, personal leave and long service leave).



- **Superannuation:** contractors pay their own superannuation, whereas employees are entitled to have superannuation contributions paid into a fund by their employer.
- **Tools:** a contractor will typically use their own tools and equipment, whilst employees are usually supplied with tools and equipment (or a tool allowance) by the employer.

Whilst the above indicators provide some useful guidance, there are some simple steps that businesses can take to try to ensure that contractors are not classified as employees:

- where possible, allow the worker to subcontract and set their own hours;
- where appropriate, allow the worker to contract with other businesses;
- never include any form of paid leave arrangement in a contractor's agreement;
- where possible, ensure that payment is by result rather than by salary or hourly rate;
- pay contractors only on receipt of an invoice and never deduct PAYG tax from their pay; and
- where possible, ensure that contractors provide their own equipment (e.g. mobile phones).

If business brokers require any further guidance, the Australian Taxation Office provides guidance to employers by an online "Employee/Contractor Decision Tool" (just search that phrase on-line to get a link). The tool guides users through a series of questions to help determine whether a particular worker is an employee or contractor. Once the questions have been answered, the tool provides the user with a report providing a "decision" regarding the worker's status, the basis of the decision and a summary of the employer's taxation and superannuation obligations relating to the worker.

If a person is classified as an employee, then there are serious consequences as the employee will have the entitlements (National Employment Standards) guaranteed under the *Fair Work Act 2009*, unless the employee is engaged on a "commission only" basis.

Sham Contracting under the Fair Work Act

Employers should note that under the sham contracting provisions of the *Fair Work Act 2009*, a sham arrangement occurs where an employer attempts to disguise an employment relationship as an independent contracting arrangement (usually done to avoid the responsibility of employee entitlements). In particular, an employer cannot:

- misrepresent an employment relationship or a proposed employment arrangement as an independent contracting arrangement;
- dismiss or threaten to dismiss an employee for the purpose of engaging them as an independent contractor; or
- make a knowingly false statement to persuade or influence an employee to become an independent contractor.

The *Fair Work Act 2009* provides serious penalties for contravention of these provisions. So unless the worker can properly be classified as a contractor, the business may have to engage the worker as an employee with all the entitlements that go with being an employee under the Act. However, there is an exception under the *Fair Work Act* that allows for "commission only" employees.

Commission Only Employees under the Fair Work Act 2009

Given that real estate agents and brokers are in a commission based industry, employers have been granted a concession by being allowed to employ real estate agents or brokers on a commission only basis, to avoid the burden of employees with standard rates of pay under an award. However, the conditions are strict and the following criteria must be satisfied:

- The employee must be at least 21 years of age and engaged as either a property sales representative or property sales supervisor under the Real Estate Industry Award 2010 ("Award"), but not engaged as a casual, junior, trainee or property sales associate.
- There must be a written agreement confirming that the employee agrees to be remunerated on a commission only basis and the basis upon which the commission is to be calculated.



- The employee must have either a real estate agent's licence or be registered or permitted to perform the duties of a real estate salesperson under real estate law.
- The employee must have been employed as a real estate salesperson for a total period of at least 12 months in the five years prior to entering into the commission only arrangement.
- Unless the employee has operated their own real estate business within the last five years, the employee must be able to demonstrate that they would satisfy the Minimum Income Threshold Test ("MITT"), discussed below.

Minimum Income Threshold Test

The MITT is a test to determine whether an employee can be engaged on a commission only basis by ensuring that employees can demonstrate from past sales experience an ability to earn remuneration by way of commission at least equal to the minimum annual award wage prescribed by the Award. It is based on any 12 month period in the last five years (so an employee's most successful 12 months would be selected). An employer can rely on any evidence supplied by the employee concerning the employee's sales in the selected 12 month period, providing the employee supplies a statutory declaration confirming the accuracy of the information.

The MITT is calculated as follows:

- (a) the gross commission for each sale effected by the employee in the chosen 12 month period and deduct from each sale GST, then (if applicable) any conjunction fees and, after those two items have been deducted, a further 10% of the remaining amount.
- (b) After (a) has been calculated for each sale, add up the total amount from all sales during the 12 month period and multiply the total sales by 35%.
- (c) The MITT is satisfied if the result in (b) is greater than the annual award wage or, where you are electing not to pay allowances, at least 110% of the annual award wage.

Once an employee can be employed on a commission only basis, the Award requires the employer to pay the employee at least 35% of the employer's net commission (i.e. gross commission less GST, conjunction agent fees and 10% of the remaining amount) for each sale for which the employee is responsible.

If two or more employees are responsible for a sale then each employee is entitled to at least 35% of each "component" of the transaction. Whether that happens to be a 30/70 split, 60/40 split or 50/50 split. The end result must be that both employees each get 35% of their component.

Employee Entitlements for Commission Only Employees

Although employers are not bound by minimum rates of pay for commission only employees, employers still have other entitlements that the employee is entitled to, such as:

- Superannuation: in addition to the minimum commission only rate.
- Allowances: unless the employee can demonstrate earnings in the MITT calculation that are greater than 110% of the annual Award wage (in which case employees can be required to cover their own mobile phone and motor vehicle costs), employers will have to pay appropriate allowances if they require the employee to use their motor vehicle or mobile phone for work purposes.
- Leave: commission only employees still accrue entitlements under the National Employment Standards ("NES") such as annual leave and personal/carer's leave.

Alternatively, if an employer has negotiated a higher rate of commission, then the employer may be able to attribute some of the commission to leave entitlements and superannuation. In this regard, employers can pay an employee some of the employee's NES entitlements in advance of their accrual and also attribute a percentage of commission towards the employee's superannuation entitlement. In practice, employers can attribute a percentage of the commission above the minimum rate of 35% towards the employee's NES entitlements and superannuation in an "all up rate"; providing they ensure that the



amount attributed in advance as part of an all up rate is equal to or greater than the amount the employee would ordinarily be entitled to under the Award.

If employers take this option, they need to be able to demonstrate on each payslip that the amount attributed to the base commission, NES entitlements and superannuation have been paid.

Conclusion

Employers must appreciate the differences between a contractor and employee; otherwise the person engaged as a contractor may be classified as an employee, which would have serious consequences for the employer as that person would be covered by the Award.

Unless the worker can properly be classified as a contractor, then the employer might have to resort to a commission only basis; in which case the employer needs to ensure that the requirements are fulfilled and observed in order to ensure that the employer is not breaching the *Fair Work Act 2009*.

In any case, business brokers should note the importance of having properly drafted contracts to deal with the rights and responsibilities of their workers, be they independent contractors or employees on a commission only basis.

This Guide is brought to you by:

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