

# The WHY realities of the ‘contractor vs employee’ debate: What's your position?

AN AXIS ACCOUNTING GUIDE

Make sure you understand the ATO guidelines so you don't find yourself in hot water at tax time.

## Why a contractor?

If you ask a contractor why they think they are contractor and not an employee, here's how they might respond:

- “I have an ABN.”
- “Everyone in my industry is a contractor.”
- “My work is short term.”
- “Not all my work is for the one guy.”
- “I have a registered business name.”
- “I have a special skill.”
- “I invoice those I work with.”
- “I signed a contract to deliver this service.”

Similarly, if you ask a business owner or employer why they think a particular person is a contractor rather than an employee, they may respond with:

- “I have his ABN.”
- “He pays his own superannuation.”
- “He’s only here for specialist skills or qualifications.”
- “He wants to be a contractor.”
- “He provides me with an invoice for his time.”
- “We signed a contract.”
- “He has his own company.”
- “We always use contractors.”

Now these people may well be acting in good faith rather than deliberately trying to ‘cheat’ the system. But the truth is, these people may be employees after all, at least according to the Australian Taxation Office (ATO).

Here are the WHYS about whether someone is a contractor or an employee.

## The 12 WHY realities of the ‘contractor vs employee’ debate

### WHY 1. If a worker has an ABN they're a contractor.

While you may believe so, having or quoting an ABN makes no difference to whether a worker is an employee or contractor for a job.

ABNs may be requested by business owners or pressure may be laid on a worker who is an employee to obtain an ABN in the belief this will make the worker a contractor. Often these

businesses attempt to disguise the employment arrangement and make it look like contracting to avoid their PAYG withholding and super obligations.

If the working arrangement is employment, whether the worker has or quotes an ABN will not make the worker a contractor.

To correctly work out whether a worker is an employee or contractor, you need to look at the whole working arrangement and the specific terms and conditions under which the work is done.

**WHY 2. Everyone in my industry takes on workers as contractors, so my business should too.**

Just because 'everyone' in an industry treats workers as contractors doesn't mean they are correct. Each case must be assessed on its own merit.

Ignore common industry practice when determining whether your worker is an employee or contractor and look to the situation at hand.

**WHY 3. Employees can't be used for short jobs or to get extra work done during busy periods.**

The length of a job (short or long duration) or regularity of work makes no difference to whether a worker is an employee or contractor.

Truth be known, both employees and contractors can be used for:

- casual, temporary, on-call and infrequent work
- busy periods
- short jobs, specific tasks and projects.

To make an accurate assessment in determining whether a worker is an employee or contractor, look at the whole working arrangement and the specific terms and conditions under which the work is done.

**WHY 4. A worker cannot work more than 80% of their time for one business if they want to be considered a contractor.**

The 80/20 rule as it is more commonly known relates to personal services income (PSI) and how a contractor:

- reports their income in their own tax return
- determines if they can claim some business-like deductions.

It's not a factor a business considers when they work out whether a worker is an employee or contractor.

**WHY 5. My business has always used contractors, so we don't need to check whether new workers are employees or contractors.**

Before new engagements, a business should always check whether the worker is an employee or contractor by examining the working arrangement.

Unless a working arrangement (including the specific terms and conditions under which the work is done) is *identical* to a previous arrangement you've already checked, the outcome could be different.

If you wrongly determine that a worker is a contractor, continuing to rely on this decision would mean the business is incorrectly treating all future workers as contractors when they are employees.

**WHY 6. If a worker has a registered business name, they're a contractor.**

A registered business name makes no difference to whether a worker is an employee or contractor for a particular job.

Just because a worker has registered their business name does not mean they will be a contractor for every job or working arrangement.

**WHY 7. If a worker is a contractor for one job, they will be a contractor for all jobs.**

The working arrangement and specific terms and conditions under which the work is completed will define whether a worker is an employee or contractor for each job.

Depending on the working arrangement, a worker could be an:

- employee for one job and a contractor for the next job
- employee and a contractor if completing two jobs at the same time for different businesses.

**WHY 8. My business will only take on contractors that way we won't have to worry about superannuation and employee entitlements. This will save us money.**

You must look at the working arrangement and in each circumstance the respective terms and conditions under which the work is done to work out whether a worker is an employee or contractor.

You can't simply make a blanket business decision to treat a worker as a contractor when they're an employee for the purpose of saving on employee on costs or fulltime equivalents (employee head count).

A business may be required to pay super for their contractors. If you pay an individual contractor under a contract that is purely for the person's labour, you have to pay super contributions for them.

**WHY 9. Workers used for their specialist skills or qualifications should be engaged as contractors.**

Taking on a worker for their specialist skills or qualifications does not automatically mean they are a contractor.

A worker with specialist skills or qualifications can be either an employee or contractor depending on the terms and conditions under which the work is done.

Qualifications or the level of skill a worker has (including whether they are 'blue collar' or 'white collar') makes no difference to whether a worker is an employee or contractor.

**WHY 10. My worker wants to be a contractor, so my business should take them on as a contractor.**

[A person's preference to work as a contractor](#) does not mean your business can engage them as a contractor.

Being an employee or contractor is not a matter of choice. It depends entirely on the working arrangement and the specific terms and conditions under which the work is done.

If you give into pressure and agree to treat an employee as a contractor, you can face penalties and charges for not meeting your tax and super obligations.

**WHY 11. He gave me an invoice, so he is a contractor.**

Submitting an invoice for work done does not automatically make a worker a contractor.

To correctly determine whether a worker is an employee or contractor, you need to look at the working arrangement in its entirety and examine the specific terms and conditions under which the work is done.

If, based on the working arrangement, a worker is an employee, submitting an invoice or being paid on the basis of an invoice will not make the worker a contractor.

**WHY 12. If a worker's contract has a section that says they are a contractor, then legally they're a contractor.**

If a worker is legally an employee, a contract saying the worker is a contractor will not make the worker a contractor at law.

Businesses and workers will sometimes include specific words in a written contract to say that the working arrangement is contracting in the mistaken belief that this will make the worker (who is an employee) a contractor at law.

If a worker is legally an employee, a contract specifying the worker is a contractor makes no difference and will not:

- override the employment relationship or change the worker into a contractor
- change the PAYG withholding and super obligations a business is required to meet.

None of these WHYS independently determine whether those working with you are legally a contractor. Getting it wrong will see you in serious deep water.

## **Workers who will always be employees**

If you hire any of these types of workers, you must treat them as an employee:

- apprentices
- labourers
- trainees
- trades assistants.

## **Workers who will always be contractors**

An employee must be a person. If you hire a company, trust or partnership to do the work, the relationship is contracting for tax and superannuation purposes.

The people who actually do the work may well be directors, partners or employees of the contractor. But they are not *your* employees.

## **It's up to you to make the right decision**

If you've hired an individual, you need to work out whether they're a contractor or employee. While [the ATO has a useful tool to help determine this](#), it ultimately depends on the specific circumstances of the working arrangement.

The key is having a clear definition of the specific work tasks the person is being engaged to perform.

For more on the WHY realities of the employee/contractor debate, and to get clear on your own position and potential risks and likely responsibilities, contact Axis Accounting on [+61 \(02\) 95691155](tel:+61(02)95691155) or via our website at <http://www.axisaccounting.com.au/#contact>.