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Are your contractors truly conducting their own business?

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Arrangements with independent contractors have again been put under the spotlight in the recent decision by the Full Court of the Federal Court of Australia in ACE Insurance Ltd v Trifunovski [2013] FCAFC 3.

Engaging independent contractors on a long term basis has always been risky business. However, until recently, it was believed that the risks could be avoided by engaging a worker through a personal company. This may no longer be the case, as this recent decision of the Full Federal Court demonstrates.

Facts

ACE Insurance Ltd unsuccessfully appealed a decision of the Federal Court that had found that five insurance sales agents were employees of ACE, despite their written contracts stating that they were independent contractors.

Two of the agents were engaged by ACE through their personal companies. The individual agents were specified as those who would provide the services, but they were not a party to the contracts. The remaining three agents' contracts contained an option to assign their rights and benefits under the contract to a corporate entity.

In coming to their decision, the Full Court examined the substance of the relationship and how it operated in practice rather than the labels applied by the parties or terms of the written contracts.

The strongest indicators of an independent contractor relationship were:

- a. the above-mentioned power to conduct a business through a corporation and to assign any such corporation the agent's rights and benefits under the contract;

- b. a power to engage persons to provide secretarial, administrative or other services to the agents at their sole expense; and
- c. a requirement that agents bear all expenses and indemnify ACE against any losses.

However, despite these indicators, the Full Court decided that the agents lacked the independence to be regarded as genuine contractors and that all of the agents were really employees of ACE.

In relation to the two agents engaged through personal companies, the interposition of the personal company into the arrangement was seen as an “insufficient obstacle” to a finding that the contractors were in fact employees. It was noted that the contracts provided for personal service by the individuals and that the personal companies could, therefore, not discharge the duties imposed by the contracts.

Ultimately, the key determinant was whether the agents were genuinely conducting a business in their own right or whether they were simply serving the business of ACE.

The agents had no capacity to accrue goodwill in their own business and, having no goodwill, they had no business which could be sold. Any goodwill which they did generate belonged to ACE and any attempt to take goodwill (in the form of customer relationships) to another firm was expressly prohibited by their written contracts. In these circumstances it could not be said that the agents were genuine contractors conducting their own business independent from ACE.

As a result of this decision, ACE was ordered to pay the agents the annual and long service leave entitlements that they were entitled to as employees.

What does this mean for businesses?

This decision certainly casts doubt over the interposition of a company as a foolproof way of avoiding an employment relationship and businesses who are engaging contractors through personal companies need to be aware that their arrangements are likely to be more closely scrutinised in the future.

The decision also demonstrates that there may be a danger in requiring contractors to abide by the principal’s policies and procedures, just as the principal’s employees are required to do. The agents were required to be trained in ACE’s training manuals and the Full Court found that this was an example of ACE exercising direct control over the agents.

Although the test for determining whether a worker is an independent contractor or an employee can be complicated because many factors need to be taken into account, the starting point is to ask this simple question: “is this contractor truly conducting their own business?”

In light of this decision, businesses should review the arrangements under which they engage any independent contractors and seek legal advice if they have any concerns about their arrangements.

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