Call them independent contractors, sub-contractors, consultants, or contract employees: whatever the term, Australian businesses have seen an explosion in the number of people working for them who cannot be legally classified as employees.

From a manager's perspective, it can appear an easy solution: reduce the number of permanent staff, and instead use contractors for projects and other peaks in workload. Contractors, for their part, have freedom, choice and typically earn more per hour than they would as an employee.

There is a widespread misconception in business that if you pay a contractor to (for example) develop a computer program or create an advertising campaign, or to work on any other project, then the business automatically owns the resulting copyright and other intellectual property rights in what has been created or developed. This is not the case, unless the business has a written agreement with the contractor to that effect.

Intellectual property is a valuable asset to any business; and companies need to ensure that they have in place appropriate safeguards to ensure that unintended consequences do not flow from using contractors. Generic contracts should not be used - they often result in disputes about what was created, and what rights are to be owned by the parties to the contract as a part of the contract price.

An agreement setting out ownership of intellectual property should be signed before commencement of the contract, or before any work is undertaken. Many businesses have been held to ransom by contractors because they have neglected to take this simple precaution.

Ownership of intellectual property developed by company employees can also be a complex issue, and employment contracts should include specific provisions dealing with ownership of copyright, inventions, patents and other intellectual property developed by employees. It should also be noted that the Copyright Act confers moral rights on authors, including rights of attribution of authorship.

Australian States introduced a number of laws governing independent contractors during the 1990s. But these laws were viewed as inhibiting the growth and freedom of independent contractors, and Commonwealth legislation designed to better regulate this sector, the Independent Contractors Act 2006 (Cth) ("IC Act"), was introduced earlier this year.

The IC Act contains two main reforms:

1. Review of unfair services contracts, and
2. Exclusion of State laws regulating particular independent contractors.
New National Jurisdiction to review unfair contracts

The IC Act overrides the application of State unfair contract jurisdictions. [1] Under the new laws, independent contractors who wish to set aside or vary an unfair services contract may apply to either the Federal Court or the Magistrates Court. [2]

What is a services contract?

A services contract is a signed agreement to perform work, between an independent contractor and a principal, both defined by legislation.

Are there limits on independent contractors able to access the jurisdiction?

The review scheme favours individuals or small companies where the directors perform the work in their personal capacity. This means that large companies would generally be excluded from the review scheme.

In addition, the review scheme does not apply where the services performed by an independent contractor are for the private and domestic purposes of the principal. [3]

When is a services contract unfair?

The Act sets out the main elements to be considered in determining whether a services contract is unfair, including:

- the relative strength of the bargaining position of the parties (or those acting on their behalf)
- whether any party was subjected to unfair tactics, undue influence or pressure
- whether the total remuneration was less than in other contracts where similar work is performed.

When considering what remuneration is fair, the Court will look at market rates and conditions in similar industries. [4] If a service contract is grossly unfair in comparison with similar contracts, the Court may vary it in part, or set it aside. [5]

New Exclusions from State and Territory Laws

Typically, independent contractors are paid at a higher hourly rate than equivalent employees. This is because the employer does not have to allow for on-costs such as:

- Income tax withholding
- Annual and sick leave
- Superannuation
- Workers compensation
- Payroll tax

The IC Act excludes State and Territory laws affecting the following terms in a services contract:

- remuneration
- leave entitlements;
hours of work of employees
- enforcing or terminating contracts of employment
- disputes between employees and employers. [6]

An employer must now negotiate all these matters with its independent contractors.

**Compliance is an issue for business**

Difficulties may be encountered in applying the IC Act to independent contractors, in determining whether their remuneration is included when calculating superannuation, pay-roll tax and workers' compensation premiums.

Whilst an independent contractor is unable to claim many entitlements which apply to employees, in certain professions, State legislation governs terms and conditions in a service contract so that an independent contractor/principal agreement can be considered to be a contract between an employee and employer.

These State provisions apply to particular workers in eastern states and may in addition define maximum ordinary hours of work.

**Are there any exceptions to the application of the IC ACT?**

Very few exceptions apply. The IC Act does set out minimum rates of pay (as part of the Australian Fair Pay and Conditions Standard) for contract outworkers in the textile, clothing and footwear industry where an outworker is not guaranteed a minimum rate of pay under State or Territory laws. Other minor exceptions are made in the IT Act. [7]

**When is the effective date?**

The laws commenced on 1 March 2007, and apply to all new contracts. This resulted in the immediate over-riding of particular State laws as set out above. However contracts entered into before 1 March 2007 will continue to apply and there is a transitional period of up to three years, unless the contract ends earlier.

**Reform Opt In Agreements**

A company can request its contractors to sign a written agreement (Reform Opt In Agreement) specifying that they are independent contractors. This has the effect of terminating the application of State or Territory laws governing their services contract. [8]

Parties to contracts dated prior to 1 March 2007 can enter into reform opt-in agreements with a three year transitional period to adjust to the new arrangements.

Companies should note that when the services contract ends, employee entitlements such as annual leave must be paid out. [9]

Principal should be aware that the IC Act specifies that it is illegal to coerce a person into signing a reform opt-in agreement, or to knowingly make a false statement in order to persuade or influence another person into signing
such agreement. In addition, it is illegal for an employer to dismiss an employee for the sole purpose of re-engaging them as an independent contractor.

The Federal Court may impose a maximum penalty of up to $6,600 for individuals and up to $33,000 for a body corporate per breach, and in addition may grant an injunction or require compensation to be paid to a person damaged by the breach.

What does this mean for business?

A prudent manager will determine whether contractors are covered by the new laws and check all services contracts to ensure compliance with the IC Act.

Current employee and independent contractor arrangements should be carefully reviewed, as heavy fines apply to sham contracting relationships. Use the common law test to determine independent contractor status.

An agreement alone does not make a person an independent contractor in the eyes of the law, and it would be sensible to assume that at some stage, the status of the people classified as independent contractors will be questioned. Do not wait until an audit. Ensure that the project or contractor assignment, and the applicants, are suitable for independent contractor status, and that accurate service contract documentation is maintained.

It is also important that management understand the rules. Independent contractors cannot be told what to do and how to do it, except in broad terms. They cannot be required to show up for fixed work hours every day. They cannot be subject to conventional performance reviews. If a business is managing independent contractors the same way they are managing salaried and hourly employees, then it should either change the approach or to reclassify the contractors.

Stephens Lawyers & Consultants have extensive experience in preparing contracts and in all aspects of intellectual property. For further information contact:

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[1] Independent Contractors Act 2006 (Cth), sub-section 7(1)(c) (other than in relation to proceedings commenced prior to the IC Act's commencement). Note Independent Contractors Act 2006 (Cth), Part 3 and section 12 where the IC Act provides for Commonwealth legislation to override State and Territory laws that previously allowed a court, commission or tribunal to amend, vary, set aside, declare void or find unenforceable terms of a services contract on an 'unfairness ground'.

[2] The contract review provision under the Workplace Relations Act 1996 (Cth) have been repealed and reinstated in the new IC Act.


[5] Independent Contractors Act 2006 (Cth), sub-section 16(2)

[6] Independent Contractors Act 2006 (Cth), sub-section 8(1)

[7] Independent Contractors Act 2006 (Cth), sub-section 7(2)


[9] Independent Contractors Act 2006 (Cth), sub-sections 35(6) and 35(8)

