Submission No 158

INQUIRY INTO NSW WORKERS COMPENSATION SCHEME

Name: Mr Doug Vorbach

Date received: 16/05/2012

NSW WORKERS'S COMPENSATION
SCHEME REVIEW
REVIEW OF DEEMING PROVISIONS

Doug Vorbach

Solicitor

REVIEW OF DEEMING PROVISIONS

Executive Summary

This short paper will discuss an area for amendment of the Workers' Compensation Scheme which is not suggested in the issues paper. This paper proposes that there be a review, or abolition, of the deeming provisions of the Scheme, by which contractors become "workers" of those who hire them. This would reduce the number of people to whom benefits are available, with an obvious financial saving to the scheme as a consequence. Such a review may also reduce the cost of employing people in NSW, making the State more attractive to new and existing enterprises, and reducing their migration to other, cheaper, States.

History

The Workers' Compensation Scheme has long contained deeming provisions. The current version is found at Schedule 1(2) of the *Work Injury Management and Workers Compensation Act* (WIM). In 2006, the scope of the deeming provisions was considerably expanded by the introduction of Schedule 1(2A) of WIM, which increased the territory of deemed employers and workers.

The original intent of the predecessors to Schedule 1(2) of WIM was to prevent employers from avoiding their obligations under the scheme by simply calling the members of their workforce "contractors". For the employer, these sham contracting arrangements reduced exposure to claims, as well as reducing overheads in the form of payroll tax and workers' compensation premiums, amongst other things. In the context of its original intention, to overcome "sham" contracting, the provisions were, and continue to be, commendable.

Modern trends in labour engagement

In more recent years, there has been a growing trend in commerce and industry of outsourcing and using contractors for the fulfilment of business needs. Offshore outsourcing is well known to all of us and its primary aim is to access cheap foreign labour to reduce the overheads of business. Of course, the other side of that coin is that the local workforce is diminished and jobs are lost here.

Business in Australia, and particularly small business, has come to appreciate the advantages of having access to independent contractors for fulfilment of their business needs. A very obvious example is the need to replace a worker on parental leave. The employer may engage a contractor for a limited period to this end. In recent times, there has been considerable inconsistency in the flow of work in the commercial sphere, the building industry, manufacturing, and retail. Rather than maintain a workforce of direct employees of sufficient size to cope with high work levels, employers are more inclined to have a relatively small core group of employees, and look to labour hire companies or independent contractors to fulfil their needs during period of high workloads.

The situation of the labour hire substitute does not require review. The labour hire worker is employed by the labour hire agency, who then on-hires the worker to the hirer. The worker is covered by the workers' compensation insurance of the labour hire company.

Another form of worker substitution is the "ODCO" form of labour management. Under this model, labour is provided by independent contractors who, through an ODCO agency, are placed with hirers who were clients of the agency. This form of contracting attracted the approval of the High Court as genuine contracting. In response, NSW introduced Schedule 1(2A) of WIM to deem the ODCO agency to be the employer of the contractors. The aim of this amendment to the Act was, principally, to ensure that Workcover received premiums in respect of the contract workers. The contractors

themselves were set up with personal disability insurance cover and were more than content with being able to manage their own affairs as independent contractors. Very few of the thousands of independent contractors who operated under the ODCO scheme have ever made claims against the hiring companies, or the ODCO agencies.

The Federal Government has recognised the legitimacy of independent contracting as part of the modern business model. Under the *Independent Contractors Act*, 2006, it has seen fit to provide some level of protection for independent contractors in respect of State workplace relations laws. Workers' compensation is excluded from the ambit of the *Independent Contractors Act*, however the intention of the Act is to prevent contractors from otherwise being treated as employees under State laws.

Contractor's perspective

For the contractors, there are numerous and significant advantages. They are able to arrange their own financial affairs and optimise their tax positions, by having access to valid business structures and business-related deductions which are not available to employees. They may have income-sharing arrangements. They may work during the hours and on the days and at the times they choose. They are their own bosses. Provided that they have adequate income protection insurance, they have a safety net in the event that they do suffer injury. Such insurance provides more extensive cover than workers' compensation, in that it will cover the contractor for injuries sustained at any time of any day in any circumstances, work-related or not.

A survey undertaken by one ODCO contracting agency showed that of those workers who had changed their status from employee to contractor, there was unanimity that they would not return to being employees, given the option. They preferred the contracting model of engagement.

Hirer's perspective

The current Scheme also may have a very detrimental impact upon businesses which engage contractors. Even though they genuinely believe that they are dealing with contractors whose payments do not need to be included in their workers' compensation wages declarations, often they are audited by Workcover, using arbitrary guidelines, and found to be deemed employers of the contractors. This has the effect of the business being the subject of a massive increase in workers' compensation premiums, often to crippling effect. Not only do they have to pay extra premiums, but they must pay the costs of the audit and they are often penalised with fines in addition. These audits usually span three years of hindsight, so there is a collection of three years of extra premium at one time, in addition to the premium for the current year. In more than one case of which I am aware, such an increase in premium and imposition of penalties as a consequence of a Workcover audit has meant that the business must be wound up. This has the consequence of New South Wales losing part of its commercial fabric; as well as the employees of that business, and the contractors, being out of work. Ironically, it also deprives Workcover of the additional premium, as well as future premiums, after having paid for a costly audit. NSW becomes less able to attract new enterprises.

Premium Review

For the business, the only recourse in the event of an adverse premium review is to apply to Workcover for a review of the premium assessment under section 170 of the *Workers' Compensation Act* (WCA). This imposes upon Workcover an inescapable conflict of interest. Workcover is the authority which manages all of the workers' compensation premiums in New South Wales, as well as payments to workers under the scheme. It is obviously in the interests of Workcover to maximise the amount of premium collected. The only recourse for an employer for a review of premium is to the Workcover Authority. Obviously, Workcover has a vested interest in maximising premiums, in order to increase its funding, without concern for the consequences to the employer.

Then there is section 172 (4) of the WCA which provides that the business must pay the premium, even if it applies to Workcover for a review of the premium under section 170. In many instances, payment of the premium will cripple the company and prevent it from being able to properly prepare a submission for review of the premium. If there is an adverse outcome from a section 170 review by Workcover, the only recourse for the business is administrative review in the Supreme Court. This is

beyond the financial reach of many smaller businesses, as the legal costs of approaching the Supreme Court are substantial, especially after having to pay the reviewed premium, audit fees, penalties and any costs associated with applying under section 170.

The Common Law test of a contractor

Currently, whether a person is a genuine contractor is determined by common law criteria which have been developed over many decades of litigation. These are set out in some detail on the Workcover website (and also the equivalent websites in every other State), but include concepts such as the control of the worker; the provision of tools; responsibility for faulty workmanship; the method of payment; deduction of superannuation and taxation; entitlement to paid sick and annual leave; and numerous others. No one test is supreme, and each situation must be judged having regard to its totality and a balance of the competing criteria.

This, in itself, creates extreme uncertainty for businesses, when faced with the decision as to whether to include contractor payments in wages declarations. To do so where there is a genuine contracting arrangement exposes the business to very substantial increases in workers' compensation premiums. A failure to do so may lead to a crippling review of insurance premiums, and penalties, after a Workcover audit. It is an untenable dilemma for business. I have seen a recent Workcover audit in which the auditor adopted a very capricious and arbitrary interpretation of the common law rules, leading to a recommendation that two genuinely independent contractors be included in the company's wages over a three year period. Assuming that the audit is accepted by the Workcover agent, the insurer, the company will be liquidated. As a consequence, the contractors will be out of work; the company's direct employees will be out of work; and Workcover will not receive the reviewed premiums, the penalties, or any future premiums, while still having to pay any current and future workers' claims. Who achieves a benefit from this scenario?

Reform

It is suggested that the Act be amended to introduce a greater certainty into the question of who is an independent contractor for the purpose of claims, and premium assessment. The obvious benefit to the scheme would be to reduce the number of people to whom benefits are available.

In the Northern Territory, a person who provides an ABN is excluded from being an employee. In Victoria, a contractor is only deemed to be an employee if the principal usually requires such work for more than 180 days per financial year; or the contract runs for more than 90 days for the one business. The Victorian scheme includes other definitions, such as the provision of labour being secondary to the provision of materials and the availability of the contractor to work for the public generally. Some of these additional criteria have been extracted from the common law tests.

It is my recommendation that some form of check list be developed to define who may or may not be an independent contractor for the purpose of the Scheme. This checklist may include items such as:

- The contractor has an ABN and is available to the public generally;
- The contractor has income protection/personal injury insurance cover;
- The contractor provides his or her own tools;
- The contractor is responsible for correction of errors in the work;
- The contract is for a defined period (less than 90 days or 180 days);
- The contractor is not entitled to paid sick or holiday leave;
- The contractor is entitled to delegate the performance of the work.

Such reforms would provide:

- Certainty and protection for those engaging contractors
- Reinforcement of the independence of contractors, while protecting genuine workers
- Reduced need for costly Workcover audits
- Simpler claims management with reduced litigation

Doug Vorbach

16 May, 2012