Submission to the ABCC inquiry: *Sham arrangements and the use of labour hire in the building and construction industry*

By the Australian Mines & Metals Association (AMMA)

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Introduction

AMMA makes this submission in response to a discussion paper released in December 2010 by the Australian Building & Construction Commission (ABCC) as part of its inquiry into *Sham arrangements and the use of labour hire in the building and construction industry*.

About the resource construction industry

Given the historically high levels of investment being poured into mining and energy construction projects as a result of the currently high demand for Australia's natural resources, it is essential that the workplace relations environment in the building and construction industry does not hinder the economic opportunities available by adding to the compliance burden for business in an already heavily-regulated environment.

There were $132.9 billion worth of resource projects in the committed stage of development as of October 2010[1], plus another $248 billion in less advanced resource projects in the pipeline. These include mineral, energy and infrastructure projects in every state in Australia. The value of committed capital expenditure associated with these projects is nearly 12 per cent of Australia's gross domestic product (GDP), while the resource industry as a whole currently accounts for nine per cent of Australia's GDP at a value of $102.6 billion[2].

The construction of new resource projects and the expansion of existing operations will be the key driver in ensuring the continuation of the resource industry's recent stellar performance. Therefore, the operation of the laws and regulations applying in the building and construction industry is critical to the continued growth of the resource industry. This is the basis upon which AMMA makes this submission to the ABCC's inquiry.

About AMMA

AMMA is the only national employer group representing the interests of the resource industry, having been serving the industry for over 90 years, particularly in relation to workplace relations issues facing employers.

[1] *Minerals and energy: major developments: October 2010*, published by ABARE, 18 November 2010
[2] *Australian Commodities Statistical Tables*, Vol 18, No 1 March quarter 2011, ABARE

The majority of resource industry employers that operate in Australia are AMMA members that employ a significant proportion of the 205,800 direct employees in the mining industry as a whole[3]. The industry is estimated to be responsible for three times as many indirect as direct jobs.

AMMA member companies are engaged in a variety of activities in industry sectors including:

- Mining;
- Hydrocarbons;
- Maritime;
- Exploration;
- Energy;
- Construction;
- Transport;
- Smelting;
- Refining; and
- Suppliers to those industries.

AMMA's Board is comprised of business leaders from:

- Alcoa of Australia Ltd;
- Anglo American Metallurgical Coal;
- Esso Australia Pty Ltd;
- Minara Resources Ltd;
- Mobil Oil Australia Pty Ltd;
- Newcrest Mining Ltd;
- Oz Minerals;
- P&O Maritime Services Pty Ltd;
- Sodexo Australia and New Zealand; and
- Woodside Energy Ltd.

[3] *Labour Force, Australia, Detailed, Quarterly, February 2011*, ABS, Catalogue no: 6291.0.55.003

Recommendations

1. The ABCC needs to collect hard evidence about the extent of the sham contracting problem, including where it is most likely to occur, before any further compliance mechanisms are introduced in this area.

2. If the ABCC is inclined to take any action following this inquiry, an aggressive and targeted education campaign should precede anything else. This could include targeting parties at the sub-sub-contractor level as well as educating individuals at the point of applying for Australian Business Numbers (ABN). Individuals could be educated about their rights, entitlements and obligations under an independent contracting arrangement as opposed to an employment relationship to ensure they are fully informed.

3. If the inquiry recommends any regulatory/ legislative changes, these should be restricted in their application to arrangements involving individuals earning less than $113,800 a year. This is in recognition of the fact that high-income earners are generally not vulnerable individuals in need of extra legal protection on top of what currently exists.

4. Allowing employers to give enforceable undertakings as an alternative to prosecution in the first instance would be a reasonable regulatory measure following evidence of the extent of the sham contracting problem being provided and an education campaign being conducted. Such a measure would require changes to be made to the Building & Construction Industry Improvement Act in order to allow the ABCC to accept such undertakings from employers.

5. 'Opt-out' arrangements could be considered whereby parties earning more than $113,800 a year could sign a statement saying they are fully informed about the independent contracting arrangement they are entering into and understand their liabilities under such an arrangement, including workers' compensation coverage and superannuation contributions.

How widespread is the problem?

Before the ABCC recommends any additional compliance burdens be placed on businesses operating in the building and construction industry, by way of legislative or regulatory change, the regulator must provide evidence of the extent of the alleged sham contracting problem.

At present, there are widely divergent views about whether sham contracting is in fact a widespread problem in the industry, with large employers and employer groups tending to maintain that sham contracting and the exploitation of workers is not widespread, while unions such as the CFMEU claim the practice is rife.

While declining to formally engage with the ABCC's current inquiry, the CFMEU has nonetheless released a lengthy report, *Race to the bottom*, alleging sham contracting arrangements in the building and construction industry are costing Australians $2.45 billion a year in unpaid taxes[4].

The CFMEU's report simultaneously seeks to undermine the credibility of the inquiry and influence its outcomes:

> *After years of prosecuting workers and unions, the ABCC's sudden interest in the issue of sham contracting is a cynical attempt to reinvent itself as an 'impartial' regulator. The ABCC 'inquiry' into sham contracting is a sham in itself.*

The report claims:

> *While legitimate contracting arrangements occur throughout the construction industry, the CFMEU has uncovered widespread sham contracting through its extensive daily interface with the industry.*

The report goes on to claim, despite providing no directly applicable figures with which to back up its assertions:

> *On the basis of official figures, it can be estimated that the number of sham contracting arrangements in the construction industry as*

[4] *Race to the bottom: Sham contracting in Australia's construction industry*. Report by CFMEU construction and general division, March 2011

> *at November 2010 is between 92,000 and 168,000. These are conservative estimates. Anecdotal evidence and industry experience suggests the real figure is much higher.*

Having made that assertion, the CFMEU concedes that the true extent of sham contracting arrangements is difficult to know:

> *Determining the exact number of sham contracts in an industry presents some inherent difficulties. Because the arrangement is designed to disguise an employment contract, the true nature of the relationship is not always immediately apparent. There are also contractual arrangements that fall well within the grey area between employment and a bona fide contract for services.*

The CFMEU's claim as to the amount of tax revenue lost to sham contracting arrangements is based on a rough assessment of the extent of the problem – derived from looking at the number of independent contracting arrangements existing in the building and construction industry and assuming a particular percentage of them are shams – then extrapolating that to arrive at an estimate of lost revenue.

It should be noted that the Fair Work Ombudsman has only taken five matters relating to alleged sham contracting arrangements to the courts in the past three years, which hardly speaks of a widespread problem. Similarly, the sham contracting provisions of the *Fair Work Act* have rarely if ever been used, again suggesting that any assumption that the problem of sham contracting is a widespread practice is itself premature.

AMMA maintains that if, as a result of the current inquiry, the ABCC seeks to impose greater compliance obligations on contractors operating in the building and construction industry, the extent of the incidence of sham contracting arrangements must be proven in more than an anecdotal way. Only then can industry stakeholders and the regulator hope to arrive at a solution that is targeted to the areas where it is needed most.

AMMA is not saying that a problem of sham contracting in the building and construction industry does not exist, merely that there is insufficient evidence of its prevalence at this stage on which to proceed with further regulation.

Anecdotal evidence from employers operating in the industry tends to suggest that if and where sham contracting arrangements do exist to the detriment of workers, it is generally at the sub-sub contractor level. If this is the case, the ABCC's targeted compliance activities, including any proposed legislative or regulatory changes, should be focused squarely at that level of operation.

Are the Fair Work Act's sham contracting provisions enough?

Protections afforded by the Fair Work Act

The *Fair Work Act's* sham contracting provisions are contained in s357, s358 and s359 of the legislation. They are intended as an adjunct to the Commonwealth *Independent Contractors Act* (which seeks to regulate independent contracting arrangements) rather than a complete legislative solution for remedying contractual unfairness. The three relevant sections of the *Fair Work Act* are reproduced below:

Section 357

Misrepresenting employment as independent contracting arrangement

(1) A person (the employer) that employs, or proposes to employ, an individual must not represent to the individual that the contract of employment under which the individual is, or would be, employed by the employer is a contract for services under which the individual performs, or would perform, work as an independent contractor.

(2) Subsection (1) does not apply if the employer proves that, when the representation was made, the employer:

a. Did not know; and

b. Was not reckless as to whether;

The contract was a contract of employment rather than a contract for services.

Section 358

Dismissing to engage as an independent contractor

An employer must not dismiss, or threaten to dismiss, an individual who:

(a) Is an employee of the employer; and

(b) Performs particular work for the employer;

In order to engage the individual as an independent contractor to perform the same, or substantially the same, work under a contract for services.

Section 359

Misrepresentation to engage as independent contractor

A person (the employer) that employs, or has at any time employed, an individual to perform particular work must not make a statement that the employer knows is false in order to persuade or influence the individual to enter into a contract for services under which the individual will perform, as an independent contractor, the same, or substantially the same, work for the employer.

These sections of the *Fair Work Act* offer broad defences to employers, aside from those employers engaged in unscrupulous behaviour designed to exploit vulnerable individuals. Although broad, the provisions are rightly focused on protecting against false and misleading statements being made by employers in order to coerce relatively powerless individuals into becoming independent contractors and thereby foregoing employment conditions and entitlements. As such, AMMA maintains that the current sham contracting provisions of the *Fair Work Act* are rightly aimed at counteracting the worst type of behaviour by employers and that these would be adequate if proactively utilised.

Some have argued it would be extremely difficult to successfully prosecute an employer under the *Fair Work Act's* sham contracting provisions given that employers could always argue they did not deliberately mislead a worker by fraudulently representing an arrangement because they themselves were ignorant of the law.

With this in mind, AMMA maintains that an aggressive and targeted education campaign should be one of the first things the ABCC considers as an action point out of this inquiry. As will be discussed later in this submission, AMMA believes the education of industry participants is paramount and should precede any other moves the ABCC might make in an attempt to eradicate the problem, such as legislative or regulatory solutions.

It is also worth noting that the current Labor Government has been adamant in its refusal to re-open the *Fair Work Act* for any stakeholder in order to enact legislative change. It is therefore very unlikely that the government will adopt legislative change in the immediate future in the event that that is what the ABCC recommends.

Tax incentives need to be addressed

While the ABCC's inquiry is a multi-disciplinary one involving knowledge sharing between the construction industry regulator and other government agencies such as the Australian Taxation Office (ATO) and the Office of the Fair Work Ombudsman, AMMA maintains that in many respects the current inquiry is one that would more appropriately be pursued by the ATO than the ABCC.

At present, there are significant tax incentives that encourage individuals to provide their services as independent contractors rather than employees. In this light, it must be acknowledged that in many cases it is the individuals themselves who present as independent contractors and want to be treated that way. In the resource construction industry, employers competing for the scarce skills and expertise of professionals such as engineers and geologists are encouraged to enter into an independent contracting arrangement because they know that the engineer or geologist can offer their services to another business very easily in the current climate.

People with scarce expertise such as construction and mining engineers want to maximise the tax advantages available from their working arrangements and will prefer to work as independent contractors. That is not to say that such arrangements are entered into fraudulently; there are many grey areas in the debate about whether someone is an independent contractor or employee, and the courts themselves often have trouble making the distinction.

AMMA maintains that in order to seriously tackle the problem of sham contracting if and where it exists, current tax incentives need to be addressed. At present, thousands of Australian Business Numbers (ABNs) are issued every week allowing people to provide their services as independent contractors. This shows there is a very real appetite by people wanting to work as independent contractors which is unlikely to be driven solely by employers seeking to avoid their obligations to employees.

Given the fact that the ABCC, like any other government agency, has limited resources to devote to its compliance role, AMMA maintains it should not be concerned with trying to regulate the tax arrangements of independent contractors in the building and construction industry but should leave that to the ATO.

Instead, the ABCC should focus its efforts on protecting vulnerable and low-paid workers who are being exploited, if and where this is occurring. AMMA does not quibble with the fact that employers engaging in exploitative behaviour should be prosecuted to the full extent of the law. However, where parties are entering into mutually beneficial independent contracting arrangements in a fully informed way, and where individuals are paid well for their expertise, the ABCC should not squander its compliance resources by getting involved.

Let the parties themselves decide

AMMA's view that independent contracting arrangements should be able to be freely entered into without third-party interference as long as both parties consent to the arrangements in an informed way is supported by a recent decision of the Federal Magistrates Court[5].

In *Vella v Integral Energy*, Federal Magistrate Rolf Driver gave his support to the argument that the type of relationship the parties envisaged when they first entered into contracts of service should be given weight when seeking to determine whether such an arrangement was genuine, given the fact there were often grey areas.

In his January 2011 interlocutory ruling, FM Driver cautioned that it was '*dangerous to assume the determination of employment can be made by some mathematical reference to a checklist*'.

While there were relevant categories the courts could apply when attempting to decide whether someone was an independent contractor or employee, i.e. notions of 'control' and 'organisational integration', the way the parties themselves defined the relationship should be given weight, he said:

> *The issue of control, whilst it may be relevant, is not determinative. Clearly, an independent contractor can be equally supervised as to the manner in which they carry out their work as can an employee. An electrician may be called in on a construction project and directed to work as part of the overall construction team and be monitored and supervised as to what to do and when to do it. That level of control will not characterise the electrician as an employee if he is running his own business and contracting for services. Control is about the reality of the situation – who is responsible for the provision and maintenance of tools and equipment; how payment is made; how that plant and equipment is operated and whether the contractor can provide labour other than his own.*

In this case, there were numerous factors pointing towards a finding that the applicant, who subsequently claimed he was an employee, was in fact an

[5] *Vella v Integral Energy* [2011] FMCA 6, 31 January 2011

independent contractor. These indicators included the invoicing and payment system the parties agreed to and adopted, the fact that the man offered his services under the banner of a partnership, the taxation arrangements that applied, the way in which business expenses were dealt with, and the fact that the partnership from time to time employed casual labour. According to FM Driver:

> *In these circumstances, the parties' expressed intention or understanding as to the nature of their relationship has relevance where the equation is otherwise finely balanced. Accordingly, the respondent contends that the identification of the relationship between the parties as that of principal and independent contractor is the one which applies.*

FM Driver went on to say:

> *… I take into account that working arrangements have been significantly liberalised in recent years and, in the more flexible working environment that now exists, it ought to be open to the parties to determine whether the relationship is one of employment or independent contract. That must be subject to several qualifications. The first is that the parties cannot turn an employment relationship into an independent contracting relationship which is a sham, for example, for the purposes of defrauding the revenue. Secondly, an employer should not be permitted to deprive a vulnerable employee of employment entitlements by attempting to dictate an arrangement of independent contract. Leaving aside taxation shams and arrangements imposed by duress and a gross inequality of bargaining power, I see no general reason to deconstruct the fundamental nature of the relationship which the parties intended.*

AMMA agrees with these findings and maintains that – in lieu of any duress, misrepresentation or significant inequality of bargaining power – parties in the building and construction industry should be free to enter into the arrangements that best suit their respective businesses.

The ABCC should not be concerned with individuals who have knowingly and consensually entered into independent contracting arrangements but later claim

they are employees and entitled to the benefit of employment at the end of a working relationship.

There are already sufficient legal remedies available under the common law, the *Fair Work Act* and the *Independent Contractors Act* for parties to seek redress if they believe they are really employees rather than independent contractors, even where they have previously agreed to the contrary. AMMA maintains that these remedies are sufficient to ensure that vulnerable employees are protected from exploitation. No further legislative remedies are warranted at this stage.

The benefit of a high-income threshold

If parties are entering into independent contracting arrangements in an informed way, and one of those parties is offering their services for in excess of a six-figure dollar amount each year, they should be free to enter into the contracting arrangements of their choice. It is only where manipulation, coercion or exploitation arises that the ABCC should exercise additional compliance powers to intervene in the arrangements.

AMMA strongly recommends that the ABCC limit the application of any proposed legislative or regulatory change arising from this inquiry to arrangements involving those earning less than six-figure dollar amounts.

Prime Minister Julia Gillard is on the record as saying that those earning more than $100,000 a year do not need the same statutory protections as those earning less[6]. High-income earners are understood to have sufficient bargaining power to protect their own interests and are generally seen as not being vulnerable to exploitation. In Julia Gillard's own words:

> *What we've recognised is the more you earn and certainly if you earn a six-figure sum, you have some ability, some bargaining power, some ways of looking after yourself in our workplaces. So we are saying, for people who earn those six-figure sums, they can look after themselves.*

AMMA agrees. The thrust of the ABCC's inquiry should not be to intervene in mutually beneficial and consensual relationships involving people earning six-figure sums, but to protect lower-paid and vulnerable workers who have no specialised skills and consequently very little bargaining power. In saying that, it is important to point out that exploitative arrangements are not attributes of independent contracting arrangements in the resource construction industry given that skills are scarce and hence very well-recompensed.

Incomes in the resource industry are historically among the highest of all industries, with average weekly earnings for mining industry employees – based on full-time

[6] Deputy Opposition Leader Julia Gillard, *Channel Seven News*, 28 August 2007

adult total earnings – currently at $2,153.70 a week (or $111,992.40 a year)[7]. This is compared to an all-industries average of $1,328.50 a week (or $69,082 a year). In the construction industry, average weekly earnings based on full-time adult total earnings are also above the current all-industries average at $1,427.40 a week (or $74,224.80 a year).

In the context of the current inquiry, AMMA recommends the observance of a high-income threshold, above which the ABCC would not exercise any additional compliance or regulatory powers. This would be in acknowledgement of the fact that the independent contracting arrangements of high-income earners are entitled to be treated with some form of legitimacy.

To maintain consistency with the *Fair Work Act*, the high-income threshold should be aligned with the current unfair dismissal threshold of $113,800 a year and be indexed accordingly.

Vulnerable workers in the building and construction industry need the legal protections they are currently afforded and AMMA maintains they are entitled to all the benefits of employment. However, any additional enforcement activities that the ABCC might undertake as a result of this inquiry should be confined to independent contracting arrangements involving those earning less than $113,800 a year.

[7] *Average Weekly Earnings Australia, November 2010,* ABS Catalogue No: 6302.0

Other solutions

Unless and until more research is done and reliable evidence produced about the nature and extent of sham contracting arrangements in the building and construction industry, the ABCC should be reluctant to increase the compliance burden that already exists for businesses, particularly head contractors, in an already heavily regulated industry.

Any solutions proposed in the wake of the inquiry should have the goal of minimising the compliance burden on business.

An aggressive and targeted education campaign

AMMA recommends that a starting point be an aggressive education campaign that informs building and construction industry participants of their rights and obligations, as well as the potential benefits and disadvantages, of entering into independent contracting arrangements.

In order to be effective, the education campaign would have to reach into the lower levels of the building and construction industry and include activities aimed at sub-contractors' sub-contractors as well as the community at large.

One possible contact point for the education campaign would be when someone is registering for an ABN. At that point, people could be informed about exactly what entitlements they were giving up when applying for work as an independent contractor so that they were able to make informed decisions. Specifically, they could be informed that as an independent contractor they would need to provide their own workers' compensation coverage as well as superannuation benefits to any employees, including themselves.

An aggressive and targeted education campaign would also have the benefit of removing some of the defences that unscrupulous employers currently have under the sham contracting provisions of the *Fair Work Act* by reducing their ability to claim they did not know the arrangement was an employment relationship rather than an independent contracting one.

Enforceable undertakings

In the event that employers in the building and construction industry are found to have done the wrong thing by entering into sham contracting arrangements to the detriment of employees, it might be appropriate to amend the *Building & Construction Industry Improvement Act* (BCII Act) to allow the ABCC to require enforceable undertakings by employers as an alternative to prosecution.

This would operate in a similar way to how the Office of the Fair Work Ombudsman currently proceeds in the first instance when employers are found to have been underpaying workers under the terms of an industrial agreement or workplace law, for example.

These enforceable undertakings could entail employers making public admissions about their behaviour, apologies to any workers affected, and commitments to complying with sham contracting laws in future.

This type of amendment to the BCII Act would be endorsed by AMMA and would probably gain the support of other industry stakeholders and the Federal Government.

'Opt-out' arrangements

Another possibility would be for parties to exchange signed 'opt-out' statements at the start of an independent contracting arrangement to ensure the parties were informed about the rights and entitlements they were giving up in return for any financial gains. This again would reduce the need for the ABCC to actively investigate arrangements that were entered into in an informed way.

It would also give employers some piece of mind that they would not be faced with backpay claims from alleged 'employees' later on down the track.

Conclusion

In AMMA's view, there is currently a lack of hard evidence about the incidence of sham contracting arrangements in the building and construction industry. While there might be anecdotal evidence about the problem, the various industry stakeholders are widely divergent in their assessment of the issue.

If and where sham contracting arrangements do exist to the detriment of employees, those employees deserve the protection of the law as it currently stands.

However, in recognition of the fact that it is not large employers that are entering into sham arrangements with the aim of avoiding their obligations to employees, the outcomes of the ABCC's inquiry must be targeted to where the problem exists. In order to do this effectively, more research is needed about the problem of sham contracting and where and how often it takes place.

The ABCC should be extremely wary of imposing additional compliance burdens on head contractors who are acting within the law and cannot reasonably be expected to be responsible for the activities of every sub-contractor on their projects.

A targeted education campaign would be the most logical place for the ABCC to start and, as discussed, could be run in conjunction with the ATO at the point of making an ABN application. This would also recognise the fact that the current tax incentives associated with independent contracting arrangements are a big part of the reason that people are entering into them in preference to employment arrangements.

After an education campaign has run its course, the ABCC could consider other regulatory measures such as allowing the parties to give enforceable undertakings or enter 'opt-out' arrangements.

Other than that, AMMA maintains that industry parties should be free to enter into the contracting arrangements they see fit as long as they are well-informed and not coerced or exploited. Given that the ABCC is an agency with limited resources, there is no need to proactively investigate arrangements that the parties are happy with where a person is earning a six-figure annual income.