HIGH COURT OVERTURNS FEDERAL COURT DECISIONS ON INDEPENDENT CONTRACTORS AND AFFIRMS IMPORTANCE OF CONTRACTUAL TERMS

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The High Court of Australia has handed down decisions in two cases regarding the distinction between independent contractors and employees. The appeals in *Construction, Forestry, Maritime, Mining and Energy Union v Personnel Contracting Pty Ltd* [2022] HCA 1 (*Personnel Contracting*) and *ZG Operations Australia Pty Ltd v Jamsek* [2022] HCA 2 (*Jamsek*) were heard together and were both allowed, in judgments that continued the line of reasoning from the recent case of *Workpac Pty Ltd v Rossato & Ors* [2021] HCA 23.

In both cases, the High Court has held that there was a clear written agreement in place and it was thus appropriate to determine the nature of the relationship between the parties by an examination of the terms of the written agreement. It was not necessary to look further to how that contract operated in practice. Employers should therefore be mindful of the importance of the rights and obligations of the parties, and make sure these are clearly set out in the written agreement and accurately reflect the intended relationship.

A copy of the High Court's decision in *Personnel Contracting* can be found here, and the decision in *Jamsek* can be found here.

THE DECISION IN *PERSONNEL CONTRACTING*

In 2020 a Full Court of the Federal Court upheld a decision of the Federal Court that Mr. McCourt, a British backpacker engaged by a labour hire company (Personnel) to work as an unskilled labourer for a building company (Hanssen), was lawfully engaged as a contractor and was not an employee.

In that case, the defining factor was a precedent set by another appellate court, the Western Australian Industrial Appeals Court (WAIAC), in a materially identical case involving the same labour hire company in 2004 in which it was held by the majority that the workers were independent contractors. The finding in that case was that there was an "Odco" arrangement.

An "Odco" arrangement is a system under which a labour hire agency engages workers as independent contractors, and hires them out to third parties. The worker is stated not to be an employee of the host business, nor the labour hire agency. The host business pays the labour hire agency for the service, and the labour hire agency pays the worker. This was the arrangement under which Mr. McCourt was engaged.

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The Full Court was ultimately not prepared to express the view that the WAIAC's earlier decision, where it found that an Odco arrangement was valid, was "plainly wrong and that it should not be followed", and was therefore bound to follow it.

Reflecting the view of the Full Court, Chief Justice Allsop stating that "unconstrained by authority, I would favour an approach which viewed the relationship between Mr. McCourt and Personnel as that of casual employment", however the Full Court considered itself bound by precedent. In reaching this view, the "multifactorial test" was applied, meaning the Full Court assessed the totality of the relationship to determine whether Mr. McCourt was an employee.

The majority of the High Court allowed the appeal in Personnel Contracting (Steward J dissenting). It was held that:

- Mr. McCourt was an employee, as under his contract his employer had the right to determine for whom he would work and he promised he would cooperate in all respects in the supply of his labour. In return, he was entitled to be paid. The right of control and ability to supply his labour was a key part of the business of the employer and the relationship between the parties;
- The fact that the parties chose to label the relationship as one of a 'contractor' did not change the character of the relationship; and
- The majority held that where parties have comprehensively committed the terms of their relationship to a written contract, the efficacy of which is not challenged on the basis that it is a sham or is otherwise ineffective under general law or statute, there is no reason why the legal rights and obligations as established in the written agreement should not be decisive of the character of the relationship.

The matter has been remitted to the primary judge for determination according to law, with the appellant seeking orders for compensation and penalties pursuant to Sections 545, 565 and 547 of the *Fair Work Act 2009* (Cth).

THE DECISION IN *JAMSEK*

In *Jamsek*, the Full Court of the Federal Court overturned a decision of the primary judge in reaching a decision that Mr. Jamsek and Mr. Whitby, truck drivers engaged by a ZG Operations Pty Ltd and its predecessors (ZG) for a period of nearly 40 years under contractor arrangements, were actually employees.

The truck drivers were originally employed as truck drivers by ZG, between 1977 to 1985 or early 1986. They were then advised that the business would only continue to use their services if they purchased their trucks and entered into new contracts as independent contractors. As a result, the drivers agreed to the arrangement and each set up a partnership with their spouse that invoiced ZG for the services provided.

The Full Court considered that past case law established that a proper characterisation of the totality of the relationship required a consideration of the totality of the relationship. This required that significant attention be devoted to the manner in which the parties actually conducted themselves over the course of their relationship. Accordingly, the Full Court considered factors such as the goodwill (or lack thereof) generated by Mr. Jamsek and Mr. Whitby's businesses, the control exercised by the business over the day-to-day activities of the drivers and the ownership of the trucks driven by the drivers, alongside the contractual terms of the written contract, in applying a multifactorial test. The Full Court also took into account the circumstances surrounding the formation of

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the contractor agreements, including the limited bargaining power possessed by the drivers at the time of the transition from employee to contractor.

The Full Court ultimately found, in attempting to ascertain the "substance and reality" of the relationship, that a proper characterisation of the relationship was one of employer and employees. This ultimately meant that ZG was exposed to liability for entitlements such as unpaid accrued leave and superannuation, as well as penalties.

The High Court unanimously allowed the appeal, and held that when ZG offered the drivers the opportunity to purchase their own trucks and become contractors, the nature of the relationship between the parties changed. From then, the partnerships rather than the individuals owned and operated the trucks, in their capacity as contractors, and the individuals were jointly and severally liable as well as enjoying the advantages of splitting the income generated with their partners.

Further, a majority of the Court found that:

- where a written agreement between the parties comprehensively regulates the relationship between the parties, the character of the relationship between the parties is to be determined by reference to the rights and duties created by the written agreement;
- the approach of ascertaining the "substance and reality" of the relationship as a "matter of impression", as undertaken by the Full Court, is erroneous and involves an unjustified departure from orthodox contractual analysis; and
- the Full Court was in error by considering the disparity in bargaining power between the parties affected by the contract.

The representatives of the drivers had also cross-appealed, contending that Mr. Jamsek and Mr. Whitby fell within the expanded definition of "employee" pursuant to s 12(3) of the *Superannuation Guarantee (Administration) Act 1992* (Cth). The High Court ruled that it would be inappropriate to determine this issue without the involvement of the Commissioner of Taxation, and remitted this issue to the Full Court to allow this to occur.

THE HIGH COURT'S REASONING

The High Court's reasoning in both of these cases establish the following principles regarding the characterisation of a relationship as one of employer / employee or principal and contractor.

Problems with the Multifactorial Test and Totality of Relationship Approach

In both decisions, the majority characterised the multifactorial test as problematic. It was stated that such a test was apt to generate considerable uncertainty, for parties and the courts, and its future use will likely be highly limited.

It was held that there may be cases where the rights and duties of the parties are not found exclusively within a written contract, such as where the contract is wholly or partly oral where it is appropriate to look at the totality of the relationship and how the parties regulated their relationship in practice. Additionally, the majority of the High Court indicated that subsequent conduct of the parties may only be considered in order to ascertain whether an agreement was a sham or whether the terms had been varied or otherwise displaced by the conduct of the

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parties. However, absent one of these scenarios, it is likely that the Court will be confined to the terms of the written agreement.

In both cases, Gageler and Gleeson JJ dissented from the majority in respect of the multifactorial test (though their ultimate orders reached the same conclusion). Gageler and Gleeson JJ had the view that the multifactorial test was sufficiently flexible, and that focusing exclusively on the terms of the contract loses sight of the purpose of the exercise, which is to characterise the relationship.

How to Approach Written Agreements to Ascertain the Legal Character of the Relationships

While the content of the written agreements has been given primacy, the parties' description of the legal character of their relationship is not determinative, or even relevant, to the characterisation of the legal relationship. Rather, the determination is a matter for the court.

This means that factors such as control are still relevant; however, it is not the detail of the actual exercise of control that serves to indicate that a relationship is one of employer and employee. Rather, it is the right of a person to control the work of the other, under the written agreement, which is indicative of an employment relationship.

Similarly, in *Personnel Contracting* the contract between Mr. McCourt and the employer established a complex suite of rights and obligations that were essential to its labour-hire business. The right of control the employer had over Mr. McCourt and Mr. McCourt's obligation to the employer, established by the written agreement, could not sensibly be said to be compatible with Mr. McCourt carrying on his own business as an independent contractor.

Bargaining Power of Workers

In *Jamsek*, the superior bargaining power held by ZG weighed heavily on the Full Court, who ruled that due to the drivers' limited bargaining power there was a diminished clear mutual intention to alter the nature and structure of the relationship between the parties, from employees to contractors.

Conversely, the High Court has held that regard may be had to the circumstances surrounding the making of a contract. However, given that the contractor agreements with the drivers came about because ZG refused to continue to employ the drivers and demanded they became contractors, which the drivers accepted, the High Court held it was difficult to see how there could be any doubt that the drivers were thereafter no longer employees.

It was ultimately held that taking into account the bargaining power of workers, when there is no suggestion of sham or some other claim that challenged the validity of the agreements made, is a 'disguised submission of sham' and was therefore disregarded by the majority.

CONCLUSION

This decision is welcome clarity for principals engaging contractors. It creates an ability for them to more easily rely on their contractual arrangements with contractors without the risk of a claim for entitlements based on subsequent conduct of the parties influencing the construction of the terms of a well-drafted written agreement. Subsequent conduct will, however, still be relevant in a claim to set aside the contract either under

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statute, or pursuant to equitable doctrines meaning that where the legal position is insufficient or inadequate a court can nevertheless provide a remedy. This is likely to be the focus of future challenges to the (mis)characterization of an independent contractor relationship.

The impacts of this case will be particularly important for the gig economy. Deliveroo's upcoming appeal against a finding by the Fair Work Commission that a driver was an employee, entitled to protection from unfair dismissal, is likely to draw heavily on the judgment of the High Court in these two decisions.

Principals also need to remain cautious where there is statutory expansion of the common law definition of "employee" including in relation to superannuation, workers compensation, work health & safety and payroll tax.

What Should You Do Now?

Considering the primacy that has been placed on the written agreement between the parties, employers should review contractual arrangements with independent contractors to ensure they now, more than ever, comprehensively regulate the relationship between the parties and properly reflect an independent contractor relationship. It should also be ensured that there can be no suggestion that the contract between the parties is a sham, or has been varied or otherwise displaced by the conduct of the parties.

Labour hire agencies who utilise the "Odco" arrangement should consider their contractual arrangements, as it is unlikely this is a sustainable model in light of the decision in *Personnel Contracting*.

Employers should also be mindful of subsequent conduct which will still be relevant in a claim to set aside an independent contractor agreement either under statute, or pursuant to equitable doctrines.

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