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EMPLOYEES vs INDEPENDENT CONTRACTORS

Understanding the distinction between contractors and employees and the re-characterisation of a contractor into an employee

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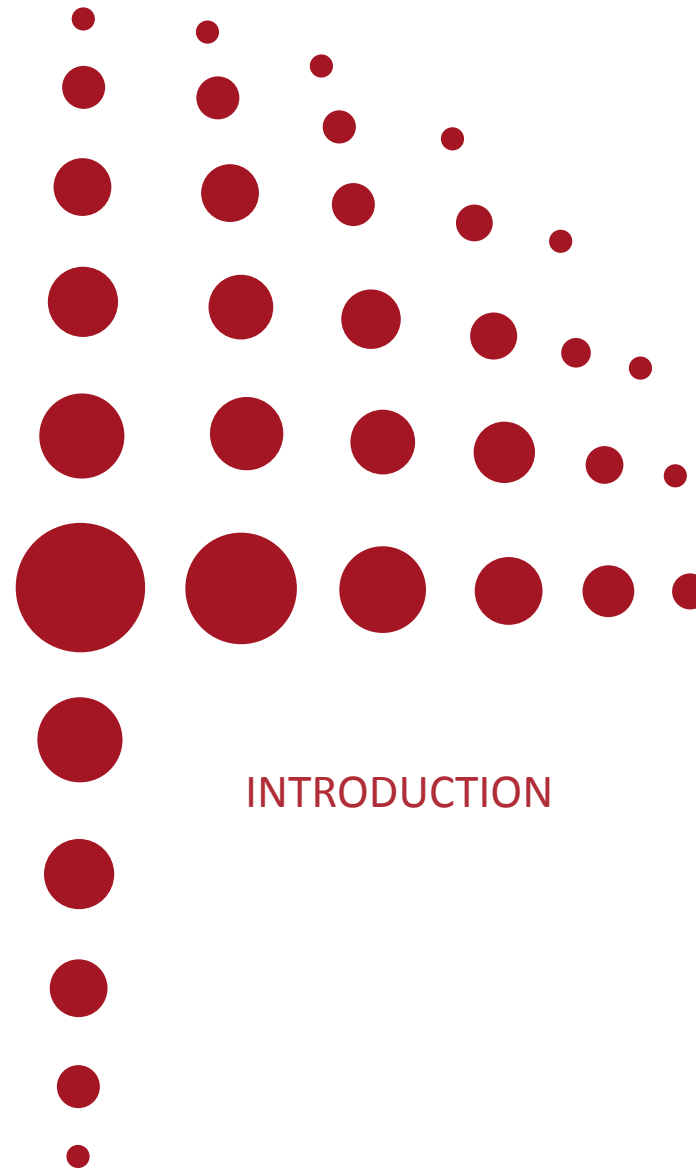
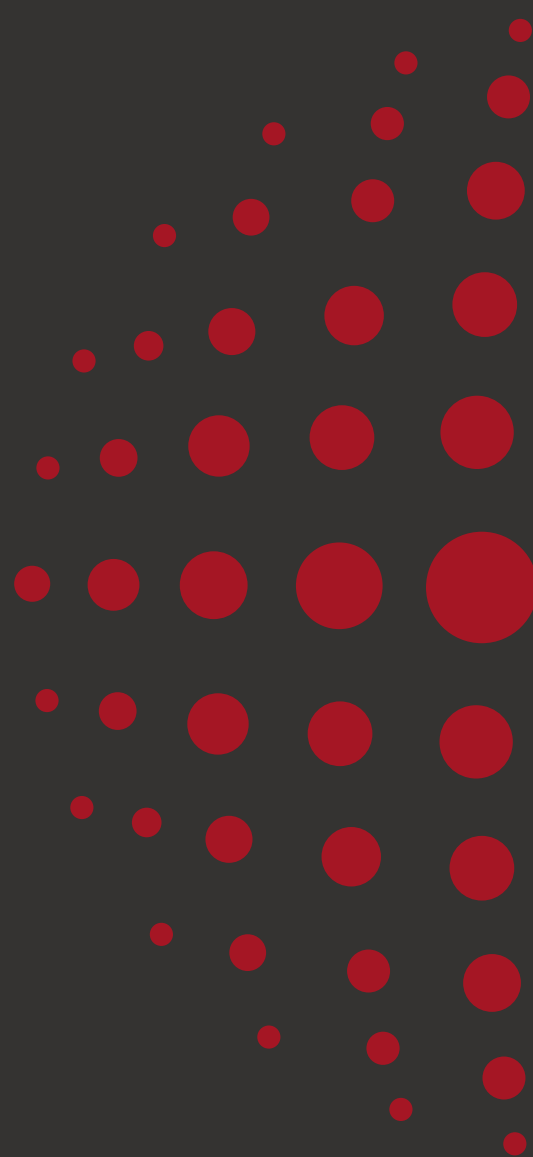
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INTRODUCTION

Since we last touched upon the issue of employees vs independent contractors and the consequences of the re-characterisation of a contractor into an employee back in 2014, there has been a universal effort to eliminate sham contracts, which seek to hide the true nature of the relationship as an employer and employee agreement. Sham contracts are generally utilised so that the employer may avert the costly burdens of guaranteeing employee benefits, such as paid leave (holiday, maternity, paternity, etc.), having to pay the employer's social security contributions and income taxes on wages, and refraining from hiring unskilled, and at times undocumented migrants, who lack the bargaining power to safeguard their rights as workers.

Despite the risks of re-characterisation, in recent years, the use of independent contractors has increased significantly. So too has the use of fixed-term contracts, temporary commercial agency agreements and labour outsourcing services. This trend is not without its faults. The rise of the on-demand sharing economy (online business transactions) in areas such as carpooling, apartment/home lending, peer-to-peer lending, reselling, co-working and talent-sharing and the enterprises that drive these new workforces, including Uber, Didi, Bpost, Airbnb, Snapgoods and Zaarly, ... has led to an increase in litigation, with the qualification of the contracts and work agreements as the central issue.

Surprisingly, there are several similarities between nations with regards to the definition of an "employee" and the classification of an "independent contractor". Generally, an employment contract is defined as an agreement by which an individual works for another person (natural or legal), under the latter's subordination, for which s/he receives remuneration. On the other hand, it is likely that an independent contract applies if an individual is responsible for organising his/her own workload and occupational activities, without being subject to the 'authority' of another.

Presented with an employee vs independent contractor situation, the most important distinction revolves around the concept of subordination, wherein the relationship is characterised by performance of duties under the authority of an employer who has the power to give orders, monitor execution of assigned duties and punish his subordinate's breaches of duties. To determine whether subordination exists, it matters less how the parties define their relationship in their agreement, but rather, the most important factor is the reality of the situation, i.e. whether or not subordination actually exists based on the actions of the parties.

Concluding that the circumstances warrant a re-characterisation (to change the status of a contractor into an employee or an employee into an independent contractor), certain legal consequences will apply, both for the self-employed person and the other party, with regards to tax (payments and arrears), social security (payments and arrears), and labour relations (civil or even criminal fines).

So what steps can an employer take to effectively establish an independent contractor relationship?

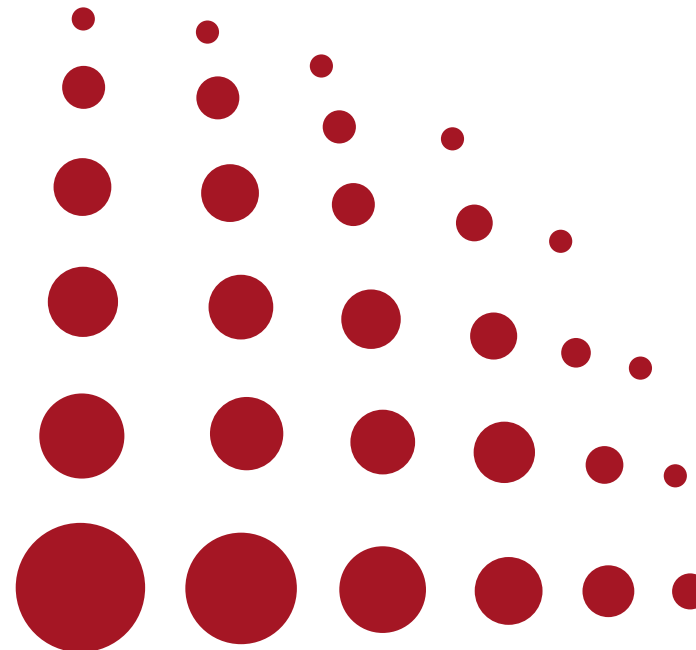
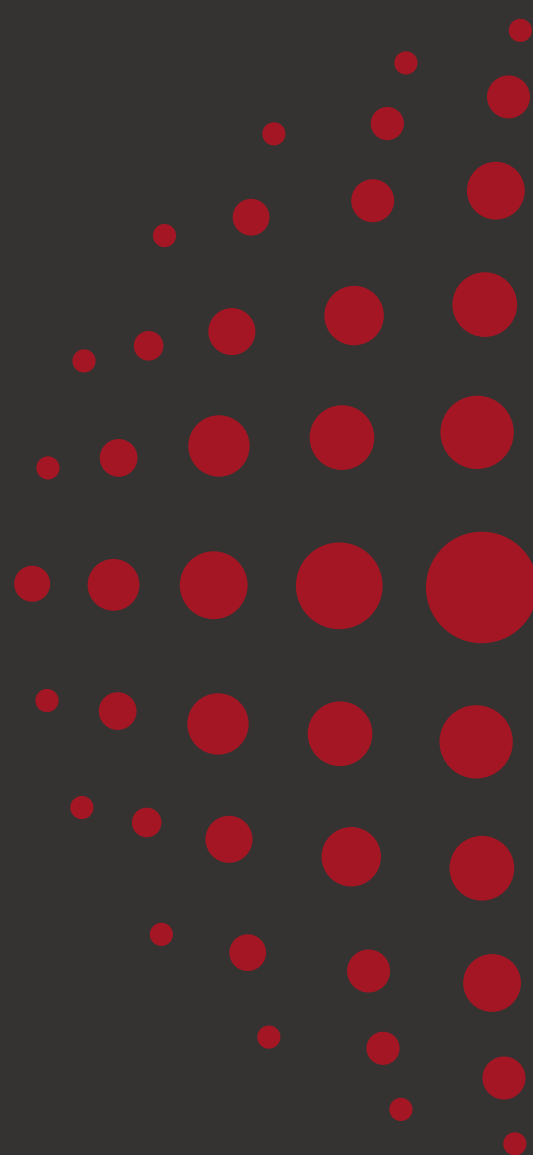
- a contract for service should be devoid of any kind of control or supervision from the principal employer or employer, as the case may be. Therefore, such employers should avoid involvement in day-to-day management of the work undertaken by the independent contractors and contract labourers.
- payment should be based on specified deliverables/results being achieved.
- limit the assignment. The agreement should not make inferences to, or guarantee, the length of assignment or future employment.
- the contractor should be free to contract with and do work for other companies.
- the nature of the services, the apportionment of risk, remedies in the event of breach, and liability for taxes, should be clearly and expressly provided for.

A well-drafted contract will not be sufficient to protect a company from an adverse finding of sham contracting. The substance of the relationship, as evidenced by its day-to-day nature, must also be maintained. The principal should therefore ensure that its managers manage the relationship with the independent contractor in a manner that is consistent with its independent nature, rather than in the same manner and with the same expectations that the Principal may have of its own employees.

Furthermore, it is important to prepare for the possibility that the nature or characterisation of a relationship may be questioned. To that end, it may be useful to keep a record of any information that supports a verbal contract or the interpretation of a written contract, this may include; email communications, notes from meetings, quotes from conversations, diary entries, lists of specifications and any form of reporting or tasks lists.

For employers with operations in multiple jurisdictions, successfully entering into a working relationship, whether with an employee or an independent contractor, is a very real challenge and one that impacts every sector of industry, in every region of the world.

To that end, L&E Global is pleased to present our 2017 Global Handbook, which serves as an introduction to the complex issue of employees vs independent contractors, with analysis from 32 key jurisdictions, across 6 continents.



ARGENTINA

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I. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTOR

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

An employee is defined by law as any individual who voluntarily renders services in favor of another within a legal, technical and economic subordination relationship, in exchange of compensation ("Employee"). On the other hand, an employer is defined as any natural individual or group of them, or legal entity that benefits from the services rendered by the Employee ("Employer").

There is not a specific definition for an independent contractor ("Independent Contractor"). However, this type of relationship is characterized by the lack of any kind of subordination. There is a legal presumption that the rendering of services implies the existence of a labor relationship, and it is the one that benefits from the services (Employer) who has to prove otherwise.

b. General Differences in Tax Treatment

Employee's Tax Treatment

The following chart shows the applicable Employee's and Employer's social security contributions and payments, respectively:

ITEM	EMPLOYEE'S CONTRIBUTION	EMPLOYER'S PAYMENT ¹
Retirement	11%	12.71% or 10.17%
Health medical services for retired people	3%	1.62% or 1.50%
Family allowances	—	5.56% or 4.44%
Unemployment fund	—	1.11% or 0.89%
Health medical services	3%	6%
TOTAL	17%	27% or 23%

Ceiling to Employees' contribution has been set at ARS 63,995.73 /USD 3,962.58 (based on the current exchange rate ARS 1=USD 16.15).

The Employer acts as a withholding agent and must withhold the Employee's contribution from wages.

In addition to the social security contributions, income tax must be withheld from the Employee's wages. Tax rates for 2016 are as follows:

ANNUAL NET INCOME (IN ARS)	TAX
0 to 10,000	9%
10,001 to 20,000	900 + 14% on amount over ARS 10,000
20,001 to 30,000	2,300 + 19% on amount over ARS 20,000
30,001 to 60,000	4,200 + 23% on amount over ARS 30,000
60,001 to 90,000	11,100 + 27% on amount over ARS 60,000
90,001 to 120,000	19,200 + 31% on amount over ARS 90,000
120,001 and above	28,500 + 35% on amount over ARS 120,000

Independent Contractor's Tax Treatment

Due to the autonomous nature of the Independent Contractor, no taxes of any kind

¹ The percentage of the employer's contribution depends on the type of enterprise. Commerce and service enterprises with invoices above a set minimum contribute the higher percentage.

shall be withheld or paid by the hiring company on behalf of the former.

Consequently, the Independent Contractor is solely responsible and liable for proper payment of any taxes, social security withholding or any other charges levied by the Argentinean authorities in connection with payments made to the Independent Contractor related to the rendering of the services described in the agreement executed between the parties.

It is not possible to give a precise amount or percentage regarding the amount to be paid by the Independent Contractor on account of his/her own taxes; it depends on the amount agreed between the parties.

If the Independent Contractor employs his/her own Employees to render services in favor of the hiring company, he/she must comply with and submit all tax filings under all applicable laws, rules and regulations to any authority having jurisdiction and pay all taxes, workers' compensation insurance premiums and any other amounts payable under all applicable laws, rules and regulations.

c. Differences in Benefit Entitlement

Employee's Benefit Entitlement

Employers must contribute to:

- Mandatory retirement and pension;
- Health care insurance; Family allowance system;
- Health medical services for retired people (Programa de Atención Medical Integral - PAMI -);
- Labor Risk Insurance (Aseguradora de Riesgos del Trabajo - ART -); and
- Unemployment fund

In addition, Employees must be paid for vacation time. Employees are entitled to an annual vacation period when they have been employed with their Employers for at least 6 months on a given calendar year.

Where the period of employment is less than 6 months in a given year, the Employee will have an annual leave equivalent to 1 day off for every 20 days of effective work.

Vacations are compulsory and the Employer must grant them between October 1 and April 30 of the next year. Its term varies according to the Employee's seniority.

- less than 5 years of service: 14 running days;
- more than 5 and less than 10 years of service: 21 running days;
- more than 10 and less than 20 years of service: 28 running days; and
- more than 20 years of service: 35 running days.

The periods of annual leave mentioned above apply unless increased benefits are established in the applicable Collective Bargaining Agreement (CBA) or in the individual employment agreement.

Employees are also entitled to a supplementary annual salary (*Sueldo Anual Complementario* - SAC -), which is paid in 2 periods during the year. Such periods have an expiration date, being the first on June 30 and the second on December 18 of each year. The amount that the Employers must pay each semester is equivalent to 50% of the best monthly salary collected in the prior 6-month term.

Employees are also provided with medical insurance for themselves and their primary

family group during the labor relationship. According to Law No.23,660, in case of termination with no cause, medical insurance is extended for an additional 3-month period following termination. However, if the insurance granted was greater than the basic plan provided by a certain healthcare company, such plan will be reduced to the basic one for the referred period of time.

The contribution to the health coverage is calculated as follows:

- 6% of the Employee's salary: paid by the Employer;
- 3% of the Employee's salary: paid by the Employee; and
- an additional 1-½% per beneficiary covered under the Employee's health coverage plan (the Employee's primary family group): paid by the Employee.

The Employee has the right to choose the health coverage to which he/she wants to contribute during the employment contract.

Independent Contractor's Benefit Entitlement

Due to his/her status, the Independent Contractor does not enjoy the legal benefits granted to the Employee. As an example, if the Independent Contractor takes vacation, it is not paid by the company that requires the Independent Contractor's services.

d. Differences in Protection from Termination

Employee's Protection from Termination

One of the main principles of the Argentine Labor Law is the principle of the continuity of the labor relationship. This principle considers that the labor relationship ends with the Employee's retirement. However, the Employer may dismiss an Employee without cause, paying statutory severance compensation established by law, and taking into account corresponding preventive measures for the dismissal not to be considered as a discriminatory act.

An Employer may also dismiss an Employee with cause, provided that the Employer can prove the grounds for the dismissal. If the Employer has evidence to establish grounds for dismissal, the Employer should not pay any compensation to the Employee.

Dismissal with cause must be the last resource after having implemented other disciplinary measures or the offense should be serious enough that it would make impossible the continuation of the labor relationship.

Legislation imposes certain requirements for dismissal with cause:

- notification of dismissal must be in writing;
- the cause and reasons alleged as the grounds for termination must be clear, accurate and detailed; and
- the alleged cause cannot be changed in successive legal notifications or during the judicial process.

In the case that the cause is challenged before the Court of Law and requirements are not met, there is a high chance that the acting judge will rule that the Employer has failed to comply with legal requirements and order it to pay severance compensation as if termination was with no cause.

Judges on termination cases must objectively evaluate: i) the facts giving rise to the dispute to determine whether there was cause for dismissal and ii) if formal requirements of notification were accomplished.

The party invoking the existence of the offense that caused the termination must submit evidence supporting such cause. However, the decision on whether the cause was sufficient lies with the judge, who analyzes the facts and evidence under the light of labor regulations and principles that govern employment relationships.

When evaluating the existence of just cause, the judge also considers:

- the proportionality of the discipline measure considering the offense committed;
- the disciplinary background of the Employee; and
- the Employee's seniority.
- Certain Employees have special protection in case of dismissals:
- Pregnant Employees within 7.5 months before or after the date of birth. If the Employer dismisses the Employee during this period, he/she shall pay severance compensation plus a fine equal to 1 complete year of compensation.
- Married Employees within 3 months before or 6 months after the marriage celebration. The Employer shall pay the same compensation as that in the case of dismissal of a pregnant employee (mentioned in the above paragraph) if he/she dismisses a married Employee during that time.
- Union representatives have a special protection granted by law in case of dismissals. They may not be dismissed if there is no prior judicial resolution to remove such protection. Officers and delegates (shop stewards) of officially recognized unions may not be dismissed from their jobs while they hold office and for 1 year thereafter. If the Employer violates this special protection, the union representative may claim the reinstatement in his/her position or consider himself/herself constructively dismissed and claim the corresponding severance compensation plus the payment of the pending salaries until the expiration of his/her period, plus a severance equivalent to a 1-year salary.
- Employee with a license for an accident or disease not related to work: If an Employer dismisses such Employee, he/she shall pay, in addition to severance compensation, the wages for all the time remaining to the expiration date of the license or to the release date, as appropriate.

Independent Contractor's Protection from Termination

Contrary to the Employee, the Independent Contractor is not protected from the termination of his/her contract.

However, in the Independent Contractor agreement, it may be established that the contract may be terminated by any of the parties, at any time, upon prior written notice sent to the other party at least 30 days in advance, irrespective of the payment of any fine and/or indemnity, for any purposes, to the other party.

In addition, either party may terminate the Independent Contractor agreement in case the other party defaults on its respective obligations and fails to remedy such default within 10 days after written notice being sent to the defaulting party for such effect, and shall bear all damages and losses caused by it.

However, considering the existence of the principle of primacy of reality, the nature of the relationship will be determined in accordance with the facts rather than by the formalities under which the relationship has been framed.

Therefore, consider that an Independent Contractor may argue that the real nature of his/her relationship is of labor kind in case there is some note of subordination note. Thus, he/she may claim statutory severance compensation plus applicable fines for wrongful registration.

e. Local Limitations on Use of Independent Contractors

There are no specific limitations on the use of Independent Contractors in Argentina. The main limitation on the use of Independent Contractors is the risk that they will be reclassified as Employees.

f. Leased or Seconded Employees

A temporary worker or leased Employee is the one provided by a temporary labor agency for short-time employment, related to temporary (not more than 6 months in a period of 1 year or 1 year in a period of 3 years) or extraordinary tasks or needs to be faced by a third company. The employment relationship will be deemed as of a temporary nature when the relationship begins and ends with the completion of the task, the execution of the act or the provision of service for which the Employee was hired. Nevertheless, the Employer who claims that the employment relationship is of a temporary nature has the burden of proving it.

The Employer of the temporary worker is the Temporary Employment Agencies (TEA), disregarding the fact that the worker may render services to different companies or even switch jobs.

A breach of the TEA regime will be viewed as a fraudulent act under local labor law. This can result in the worker being deemed to be a direct worker of the company that directly benefits from his/her service, i.e. the user company.

There must be a "reasonable and justified" balance between the number of workers hired through TEAs and the user company's permanent personnel, as well as an "adequate" term of employment. The guidelines to determine such limitations for each activity must be established by the applicable CBA.

Non-compliance with this obligation means that the agency worker will be deemed to be directly employed by the user company. Thus, the user company will be obliged to register the worker on its payroll.

In addition, the user company will be directly liable for all labor and social security obligations derived from the employment relationship.

TEAs must have an exclusive corporate purpose of supplying industrial, administrative, technical or professional staff to third-party companies (user companies) in order to:

- perform, on a temporary basis, extraordinary services defined in advance; or
- meet the specific and temporary needs of the user company.
- User companies may engage workers through a TEA, only if needed, in the following circumstances:
- to cover the absence of a permanent worker, during the term of his/her leave of absence;
- leave of absence of a permanent worker, legal or contractual suspension due to strike or force majeure, reduction or absence of work;
- in the event of increased business activities of the user company, requiring more workers, on an exceptional and extraordinary basis;
- to organize and/or participate in congresses, conferences, fairs, exhibitions or programmes;
- to perform urgent tasks to prevent accidents or repair equipment when such duties cannot be performed by regular staff; and
- when, due to extraordinary or temporary needs, tasks not related to the usual business activities of the user company are required.

With respect to the circumstances described in i) and ii) above, the name of the worker who is on leave must be specified in the agreement and, if the replaced worker returns

to his/her position and the worker hired through a TEA is still working, he/she will be considered a direct worker of the user company.

Regarding the circumstances described in iii), iv), v) and vi), the hiring period must not exceed 6 months in a 1 year period, or 1 year in a 3 year period. If the hiring exceeds these limits, the worker may be considered a direct worker of the user company.

Therefore, to hire workers through a TEA, the user company will have to provide evidence that the hiring satisfies one of the extraordinary circumstances discussed. In the case of non-compliance with the legal requirements, the worker may claim that the user company has fraudulently used the TEA to avoid correct labor registration in violation of local labor laws and claim to be correctly registered by the latter. If the user company refuses to do so, the worker may be considered constructively dismissed and claim severance compensation, plus applicable fines for incorrect registration.

Agency workers do not have special protection against dismissal. They have the same rights as other Employees engaged under contracts for an indefinite period of time. Claims for dismissal would be brought against the TEA since it is considered to be the Employer of the agency worker. However, both companies are joint and severally liable for labor and social security obligations.

g. Regulations of the Different Categories of Contracts

Labor relationships are, mainly, governed by the National Employment Law ("NEL") - Law No. 20,744 -. Argentine labor regulation is characterized by its protective nature.

The NEL covers the majority of labor relationships in their different modalities and the consequences thereof such as, compensation; annual vacation and special leave of absence provisions; holidays and non-working days; daily and weekly working and resting hours; special provisions for women and children; illness; the transfer of the labor contract; its termination; Employee's privileges, etc. Certain activities such as civil service (public sector employment), domestic and rural work are excluded from the NEL and are governed by special laws.

In addition, labor relationships are governed by the following regulations:

- Law No. 24,013: It regulates, *inter alia*, i) temporary personnel service companies, ii) the protection of unemployed workers and iii) applicable fines and penalties for incorrect registration of labor relationships;
- Law No. 25,877: It amended relevant issues regarding the individual labor relationships, which, mainly, are the following: i) trial period; ii) prior notice, iii) severance payments due to dismissal with no cause and iv) promotion of employment;
- The social security system and institutions (i.e. pension funds, family allowances, schooling allowances and health social welfare) are contained in a number of different provisions;
- Labor Risks Law (Law No. 24,557): It has created a new indemnification system for labor accidents and job-related illnesses and it has been modified and complemented by Decree No. 1,649/2009 on Upgrade of Disability Compensation; Resolution No. 35,550 on Civil Liability Insurance for Occupational Accidents and Diseases; Law No. 26,773 about a New Regime to Organize the Repair of Damage Caused by Occupational Accidents and Diseases; Decree No. 49/2014 on New Illnesses incorporated to the Official List of Occupational Diseases and Decree No. 472/2014 regulating Law No. 26,773; and
- Wage scales and other specific conditions are also ruled by CBAs, negotiated between the chambers of commerce of certain industry sectors and union representatives.

Independent Contractors are subject to a different regulation, far less protective than the Employee's one. They are governed by civil and commercial laws, which have been grouped within a unique code, since 2015.

II. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Argentina is an "Employee friendly country" and protective principles govern employment relationships. Please find below a brief of each one:

i. Protective principle: Argentina labor regulation is characterized by its protective nature. This protective nature is based on the fact that the legislator has considered the Employee the weakest part in the labor relationship. Due to this lack of equality in the negotiation power, the protective principle, the core of Argentine employment case law and regulation, was enacted.

The mentioned principle involves both individual and collective employment relationships. The application of this principle tends to balance the preexisting differences between the Employer and the Employee, and it is expressed in 3 rules:

- in case of doubt, the criterion most favorable to the Employee must prevail;
- application of rule of law that favors the Employee the most; and
- application of the most beneficial condition.

ii. Public order: rules imposed by the Argentine labor regulations are mandatory and may not be waived by agreement of the parties.

Terms of individual labor agreements that establish less rights or benefits than those established by applicable law or CBAs will be void and automatically replaced by the more beneficial terms as established by law or CBA. Any modification must always be made to increase an Employee's rights and not to reduce them.

iii. Principle of primacy of reality: the nature of a certain relationship will be determined in accordance with the facts rather than by the formalities under which the relationship may be framed. According to this principle, facts prevail over formalities.

iv. Territorial principle: the law of where services are rendered applies, disregarding any other agreement about jurisdiction made by the parties.

v. Based on the protective nature of labor regulations, all documents should be in Spanish, in addition to any other language that the Employer wishes to use.

vi. Continuity of the labor relationship: it considers that employment agreements are meant to be for an indefinite period of time, which means that they are intended to last until the individual is under conditions to apply for state granted retirement.

vii. Non-discrimination principle: Employees may not be treated differently based on sex, religion, nationality, marital status, race, political opinions or physical appearance.

b. The Legal Consequences of a Re-Characterisation

In Argentina, there is a presumption according to which the render of services in favor of another individual implies the existence of a labor relationship. Thus, in case of conflict, it is on the company (beneficiary of the services) to prove that the relationship was of

commercial nature, which is difficult due to the protective nature of local regulations.

In view of the above, when entering into Independent Contractor agreements, it is important that the hiring company is aware that the individual hired may construct an employment relationship if evidenced that:

- he/she performs tasks in favor of the company or individual regularly and on an exclusive basis;
- he/she complies with a regular time schedule and with company's instructions;
- he/she renders services in a facility and with elements/tools supplied by the company;
- the compensation he/she receives in exchange of his/her services is his/her main source of income; and/or
- he/she receives similar benefits as Employees.

Sometimes there are doubts about the existence of a labor relationship. Argentine social security authorities refuse the autonomous/commercial nature of certain relationships understanding that these relationships constitute a fraud to local labor laws and thus, a wrongful registration of a labor relationship. All cases should be resolved taking into account the principle of primacy of reality explained above.

If subordination notes may be evidenced but the company has not entered into an employment agreement, the contractor will argue that the company failed to properly register the labor relationship and request its correct registration. If the company fails to do so or denies the existence of a labor relationship, the individual may consider himself/herself constructively dismissed by fault of the company and claim statutory severance compensation together with applicable fines for non-registration.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

If an individual seeks Employee status, he/she must file a complaint against the individual or company he/she considers his/her Employer. As a first step, the Independent Contractor seeking Employee status must notify about his/her intention to be re-categorized as an Employee, requesting the registration of his/her labor relationship within the next 30 days counted from the reception of the legal notification.

The Employer has two options before a contractor's claim:

- employer registers the employment relationship reflecting the real conditions of the relationship. It is important to point out that such cases are very unusual.
- employer fails to register the labor relationship or denies the existence of a labor relationship. On this occasion, the individual may consider himself/herself constructively dismissed by fault of the company and claim severance compensation (explained below) together with applicable fines for non-registration (please see *Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterization* below).

Mandatory severance compensation for termination with no cause and final liquidation, include the following concepts:

i. Seniority compensation: this compensation is equivalent to a monthly salary times per year of services or fraction over 3 months. Such basis has a maximum cap amount provided by the applicable CBA which is 3 times the average of all wages provided by such CBA and a minimum cap amount which is 1 Employee's gross monthly salary. The application of any cap amount to the seniority compensation could be challenged by the Employee on grounds of disparity between such cap and the real salary. The Supreme

Court established that the calculation base may not be reduced more than 33%, considering such reduction as a confiscatory act if the mentioned percentage is exceeded. Therefore, fixing the cap, it must be verified that at least the calculation is made with 67% of the employees' monthly compensation in case it exceeds the cap established by the applicable CBA.

ii. Severance in lieu of notice: the NEL provides that the Employer must give a prior written notice to the Employee in the event of a wrongful termination of employment. If the Employer does not give such prior notice, it must pay compensation in lieu of notice equivalent to 1 or 2 monthly salaries, depending on the Employee's seniority;

iii. Pending days of the termination month: if the dismissal does not take place in the last day of the month, the Employer must pay a compensation equivalent to those pending days to complete the entire month;

iv. Severance for proportional vacations: disregarding the cause of termination, the Employee is entitled to compensation equivalent to the vacation pay in proportion to the days effectively worked;

v. Proportional semi - annual bonus: the Employer must pay an annual bonus ("SAC") in 2 instalments (June 30 and December 18) equivalent to 50% of the best monthly salary earned in the prior 6 month term and whatever the cause of termination of employment, the Employee is entitled to the proportional amount of the SAC;

vi. Statutory annual bonus over severance in lieu of notice: Court decisions have ruled that the Employee is also entitled to 1/12 of the amount provided for severance in lieu of notice; and

vii. Wages due - other benefits: the Employer must pay any pending salary and any other benefits, incentives, compensations due to an Employee if applicable.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

If the Independent Contractor argues the existence of a subordination relationship and claims for the correct registration of his/her labor relationship before the company terminates the relationship or communicates its decision not to renew his/her contract and the company does not comply with such registration, the Independent Contractor may consider himself/herself constructively dismissed and claim the payment of mandatory severance compensation and fines for incorrect registration: equal to: i) 1/4 of the compensation accrued since the beginning of the labor relationship, and ii) the double of severance on account of seniority, prior notice and pending days of the termination month.

In the case the company communicates its decision to terminate the relationship before the Independent Contractor claims for correct registration of his/her relationship, he/she may claim a fine equal to double that of the seniority compensation based on the labor nature of the relationship. This fine cannot be accumulated to one established in the above paragraph.

In addition, if the Employer does not comply in due time with the payment of the mandatory severance package, the Employee may claim for interest and fines, in which case the Employer must pay an additional compensation equal to 50% of the severance on account of the seniority, prior notice and pending days of the termination month.

Also, the Employer has the obligation to deliver the Employee working certificates within

30 running days from the termination of the employment relationship. If the Employer fails to comply with this obligation, the Employee is entitled to claim an additional fine equal to 3 monthly salaries. Thus, since there is no registration of the labor relationship, in case of a conflict, the Independent Contractor may likely also request this fine.

The statute of limitations applicable to labor obligations is of 2 years.

Moreover, if the Employee's claim is accepted, in addition to the explained above fines, the Employer will be sentenced to the following penalties:

- Social Security: National Tax Authority (*Administración Federal de Ingresos Públicos AFIP*-) may also claim to the Employer that it did not comply with the deposit of corresponding social security withholdings and claim the amount accrued as capital, plus fines up to 200% of the capital owed and monthly interests of approximate 2%.
 - The statute of limitation for this claim is 10 years.
- Union Matters: Eventually, if the activity rendered by the Independent Contractor is governed by any particular CBA, the corresponding union may claim the contributions not made. The percentage depends on the applicable CBA, but in general is between 2% and 5% of the monthly compensation.
 - The statute of limitation for this claim is 5 years.

III. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

We recommend that the Independent Contractor agreement is reviewed by local experts in order to ensure that its wording does not reflect any subordination note and complies with local regulations.

In addition, it is advisable to enter into an independent service agreement in Spanish or in a double column format using English/Spanish languages due to the fact that in case of a conflict of a labor nature, a Court of Law will dismiss documents drafted in a foreign language.

b. Day-to-Day Management of the Relationship

In order to minimize risks of re-characterization, it is important to:

- ensure that services are rendered on a non-exclusive basis;
- avoid i) grant of corporate tools, ii) use of corporate email address, iii) correlative invoices, iv) fixed monthly fees, v) contractor's participation in companies compensation/benefit policies, vi) compliance with fix working schedules, vii) control over the independent, and viii) orders or instructions (replace them for suggestions).

The mentioned tips will not prevent filing of a claim but, if met, they will contribute to set up a defense strategy and place the company in a better negotiation position in order to get a settlement.

IV. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

The use of one or more Independent Contractor does not create a permanent establishment in the country. Indeed, foreign companies usually execute Independent Contractor agreements without local presence in Argentina when they need an individual to render services for them locally.

It is important to point out that in order to establish a local presence in Argentina, a special procedure must be complied with (further details of such procedure will be explained below).

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

In order to be registered as an Employer before the Register of Commerce, the company must establish a local subsidiary or branch.

While foreign companies are governed as to their existence and form by the laws of its country of incorporation, when settling a branch in Argentina, they must be registered in the Public Registry of Commerce. Otherwise, it is not possible to register as an Employer.

Procedure before the Public Registry of Commerce: At this first step the company must submit a series of corporate documentation required by such Registry considering the type of company that is intended to incorporate.

As for timing concerning the process of incorporating a local branch or subsidiary before the Public Registry of Commerce it usually takes from 1 to 2 months, depending on whether the Public Registry of Commerce makes any observation to the filing and requires further clarifications.

Procedure before the local tax authority ("AFIP"): Once the registration process before the Register of Commerce is done, the company must register as an Employer before the AFIP by filing in a form. The legal representative must do such procedure.

Once this is completed, the company will be able to obtain a tax code to run their business before the AFIP and with such code it will be able to register as an Employer. This procedure will take approximately 2 weeks.

Procedure before the local social security authority (*Administración Nacional de Seguridad Social –ANSeS* -): The ANSeS is the national agency responsible for Social Security policies. Among its functions are granting pensions, family allowances for active workers and retired ones, unemployment benefits and implementing various programs of Social Security. Employers, when hiring Employees, must take the deductions and contributions to the social security system into account.

Procedure before the National Direction of Personal Data Protection (DNPDP): The National Direction of Personal Data Protection (*Dirección Nacional de Protección de Datos Personales* - DNPDP-) is the national authority that controls the traffic of personal data/information.

The DNPDP has under its supervision the Register of Data Base, an instrument created

with the aim to control the traffic of personal information.

It handles any complaint that an individual files due to an inappropriate use of his/her personal information.

In this sense, its function is to investigate whether the database complies with the principles established by law and other regulations.

The DNPDP informs about:

- the existence of a database;
- why that database requires that information and what is its aim; and
- the name and address of the individual responsible for the database.

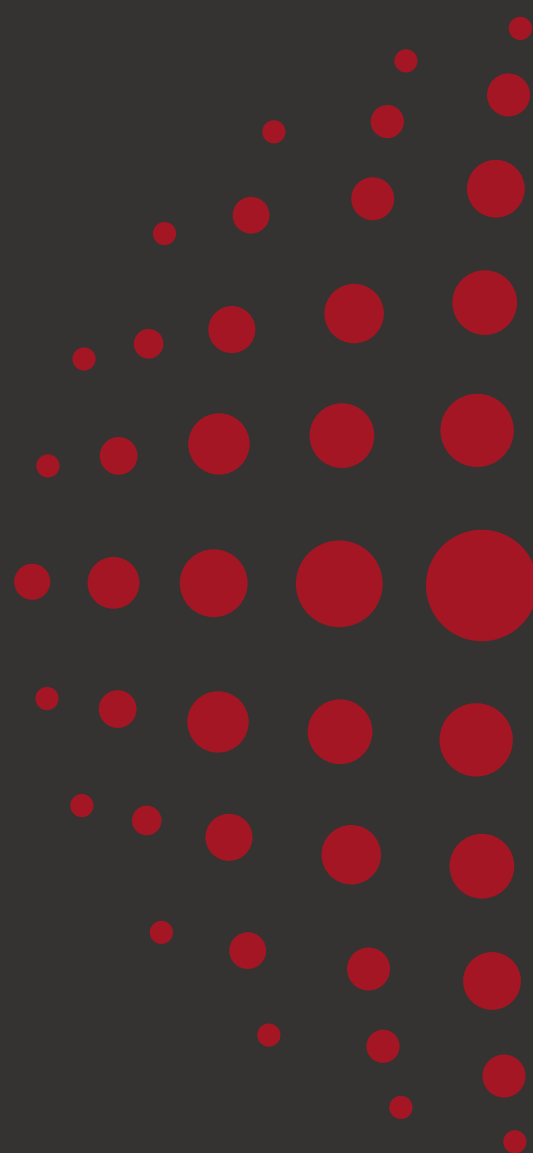
V. CONCLUSION

To conclude, both an “Employee” and an “Independent Contractor” is submitted to a specific regulation.

The Employee engaged in a **subordinate relationship** with the Employer will actually be given more advantages and protection while the Independent Contractor’s regime, although much more flexible is **undoubtedly** less favourable **in some ways**. Due to the lack of a legal framework of the Independent Contractor, it is a preferred option in particular for foreign companies with no local presence in Argentina.

Nevertheless, without prior and qualified advice the risk of misclassifying an independent contractor relationship into a subordination relationship is high and the consequences are severe. In view of that, it is important to bear in mind: i) the special protective characteristic of the Argentinean labor regulation; and ii) the subordinations notes which are the key element to construct and prove the statute of Employee to minimize the risk of misclassification of the Independent Contractor.

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AUSTRALIA

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I. OVERVIEW

This article provides a thorough outline of the law, rules, appropriate structures and trends affecting employment and independent contractor arrangements.

Part II of the article discusses the legal framework regulating contract and employment arrangements in Australia, whilst part III discusses the practical aspects of re-characterisation and its associated legal risks and exposures.

Part IV identifies and discusses the appropriate structures and methods of structuring independent contracting arrangements. Finally, part V of the article looks at recent trends and the future direction of the regulation of employment and independent contractor arrangements in Australia.

a. Introduction

Employees and independent contractors in Australia separately enjoy benefits, and owe duties and liabilities that are unique. Independent contractors are, in effect, small businesses and therefore they are not protected from unfair dismissal,¹ nor are they entitled to receive employment benefits provided under statute and other industrial awards, including annual leave and superannuation. In addition, companies that engage independent contractors may be insulated from public liabilities arising from the conduct of their contractors,² insure their contractors for injuries sustained in the course of employment³ and have significantly reduced administrative obligations in relation to reporting and record keeping.⁴

For these reasons, together with increasing labour costs, independent contracting arrangements are attractive to businesses seeking to maintain competitiveness and labour flexibility in the Australian market.

However, due to the scope for exploitation and diminished responsibility, Australian regulatory bodies have, as a matter of public policy, adopted a strict position against the misuse of independent contracting arrangements in the private sector⁵ and Australian Courts have followed their example through the imposition of increasingly large penalties against companies and managerial staff for engaging in sham contracting practices. Additionally, statutory entitlements and protections for employees have provided scope for Courts and Tribunals to award significant damages and compensation to persons that have been mischaracterised as independent contractors.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. The General Distinction Between Employees and Independent Contractors

An employment contract is accepted as a form of agreement between an employing company and an employee whereby the employee, in return for consideration in the form of regular salary or wages, undertakes to provide services to a business through the provision of their personal labour.⁶ Conversely, an independent contractor is a person who conducts a business through which they provide a service or services to a principal

¹ S. 382, FW Act

² *Hollis v Vabu Pty Ltd* (2001) 207 CLR 21

³ *Australian Air Express Pty Ltd v Langford* (2005) 147 IR 240; *Stevens v Brodribb Sawmilling Company Pty Ltd* (1986) 160 CLR 16

⁴ Part 3--6 Fair Work Regulation 2009 (Cth)

⁵ Office of the Fair Work Ombudsman, June 2015: A report on the Fair Work Ombudsman's Inquiry into the labour procurement arrangements of the Baiada Group in New South Wales

⁶ *ACE Insurance Ltd v Trifunovski and Others* (2013) 209 FCR 146, 150; *Marshall v Whittaker's Building Suppl Company* (1963) 109 CLR 210, 214-5

for the benefit of their own commercial enterprise.⁷

The distinction between employers and contractors at common law has therefore been described as being “*rooted fundamentally in the difference between a person who serves his employer in his, the employer’s, business, and a person who carries on a trade or business of his own.*”⁸

The jurisprudence in Australia, consistently with most other countries, recognises that it is a fundamental characteristic of an employment relationship that a person employed is subservient to their employer and must carry out any duties reasonably required of them. Consequently, the Courts will imply the existence of terms of fidelity and loyalty in all contracts of employment such that “*where a person has entered into the position of servant, if he does anything incompatible with the due or faithful discharge of his duty to his master, the latter has a right to dismiss him.*”⁹

On the other hand, the very nature of an independent commercial enterprise “*will usually involve the acquisition and use of both tangible and intangible assets in the pursuit of profit*”¹⁰ and therefore no such duties of fidelity and loyalty arise.

Put more simply, the distinction can be described in terms of a contract for the provision of services, or a contract of service.¹¹

b. The Legal Test for Distinguishing an Employment from an Independent Contracting Relationship

The legal definition of ‘employment’ is not prescribed in Statute, but rather derives from a range of common law tests developed principally to establish vicarious liability in tort.¹² The relevant test is multifactorial,¹³ seeking to determine “*whose business the putative employee was toiling*”¹⁴ by reference to the “*totality of the relationship.*”¹⁵

In order to determine the above question, the multifactorial ‘totality’ test requires an examination of indeterminate indicia of employment and contractor relationships, considered by authorities as assisting an enquiry into the true nature of the contractual relationship and its terms.¹⁶

Indicia of Employment Relationship

- the organisation for whom the work is performed has the right to direct the manner of performance of the work, so far as there is scope for such direction;

⁷ Stevens v Brodribb Sawmilling Co Pty Ltd (1986) 160 CLR 16, [37]

⁸ Marshall v Whittaker’s Building Supply Company (1963) 109 CLR 210, 217 per Windeyer J; cited with approval in Hollis v Vabu Pty Ltd (2001) 207 CLR 21, 39; ACE Insurance v Trifunovski (2011) 200 FCR 532, 543

⁹ Concut Pty Ltd v Worrell (2000) 176 ALR 693, [25], citing Pearce v Foster (1886) 17 QBD 536, 539

¹⁰ On Call Interpreters and Translators Agency Pty Ltd v Commissioner of Taxation (No 3) (2011) 279 ALR 341, [210]; Minister for Employment and Workplace Relations v Gribbles Radiology Pty Ltd (2005) 222 CLR 194, [39]

¹¹ ACE Insurance Ltd v Trifunovski and Others (2013) 209 FCR 146, 150; citing with approval Sweeney v Boylan Nominees Pty Ltd (2006) 226 CLR 161, 173

¹² ACE Insurance v Trifunovski (2011) 200 FCR 532, 543. S. 12(3) of the Superannuation Guarantee (Administration) Act 1992 (Cth) provides the following general definition of employment for the purposes of that Act: “[I]f a person works under a contract that is wholly or principally for the labour of the person, the person is an employee of the other party to the contract.”

¹³ On Call Interpreters and Translators Agency Pty Ltd v Commissioner of Taxation (No 3) (2011) 279 ALR 341, [204]

¹⁴ ACE Insurance v Trifunovski (2011) 200 FCR 532, [35]

¹⁵ Hollis v Vabu Pty Ltd (2001) 207 CLR 21, [24]

¹⁶ Stevens v Brodribb Sawmilling Company Pty Ltd (1986) 160 CLR 16, 24 and 36-37; Hollis v Vabu Pty Ltd (2001) 207 CLR 21, 42-45; Sweeney v Boylan Nominees Pty Ltd (2006) 226 CLR 161, 172-173. The test has been described as an “elephant test”, meaning “an animal too difficult to define but easy to recognise when you see it”, see On Call Interpreters and Translators Agency Pty Ltd v Commissioner of Taxation (No 3) (2011) 279 ALR 341, [205], citing Lord Wedderburn (1986): The Worker and the Law (3rd ed.), Penguin Books Ltd, p. 116

- the commercial risk is borne by the organisation, as is the responsibility for any loss occasioned by poor workmanship or negligence by the employee;
- the organisation prescribes the times and locations for the performance of the work;
- the remuneration is in the form of a salary or wages;
- personal income (PAYG) tax is deducted by the organisation when paying the worker;
- the organisation provides the equipment and materials for the work;
- any use of the worker’s own equipment or materials is compensated by the reimbursement or by an allowance;
- the organisation has discretion in relation to task allocation and termination of the engagement;
- the worker cannot perform similar work for other organisations;
- the worker is presented to the public as being part of the organisation;
- the worker has no inherent right to delegate their work to another, though there may be power to delegate some duties to other workers; and
- the worker receives benefits such as annual, sick or long service leave.

Indicia of a Business

- the contract is for a given result, rather than the mere provision of labour on an ongoing basis;
- the worker maintains a high level of discretion and flexibility as to how the work is to be performed, even if the contract contains precise terms as to the material to be used and the methods of performance;
- the worker bears the risk of the commercial loss or profit from the job, and the responsibility and liability for any poor workmanship sustained in the performance of the task;
- the worker sets their own hours of work;
- the worker provides their own equipment and assets;
- the contract does not include provisions for the worker to take paid leave;
- payment is predicated upon satisfactory performance of the contract;
- the worker supplies an invoice for payment and / or quotes an Australian Business Number;
- the worker is responsible for their own expenses;
- the worker is expected to insure against the risk of being injured at work, and / or the risk of causing loss to others in the course of performing the work;
- the worker advertises their services to the public at large and accepts work from other parties;
- the worker has a power to delegate or sub-contract performance of the work to others; and
- the worker is capable of accruing goodwill in their own business through their performance of work for the organisation.
- The above lists are certainly not exhaustive and each case will be decided on its own circumstances. Ultimately, the courts will assess the totality of the workplace relationship to determine whether the worker is, on balance, an independent contractor or an employee.¹⁷ Below is a more detailed look at the relevant indicia.

Control

The level and degree of control exercised by one party over the other is the most significant factor affecting the characterisation of a relationship. “Control” refers to things such as supervision and direction given as to how work is to be performed, and includes the authority to control work (as opposed to actual control). Generally, the greater the level and degree of control exercised by one party over the other, the more likely the relationship is to be characterised as an employment relationship.

¹⁷ See n. 16, Lord Wedderburn (1986)

However, it is important to bear in mind examples in which, despite workers enjoying significant autonomy and choice regarding their hours and operational elements of their job, the fact that the organisation took ultimate responsibility for quality at all stages of the production process demonstrated a sufficient degree of control to establish an employment relationship.¹⁸

Mode of Remuneration

There is a notable and indicative difference between the modes of remuneration for an employee as opposed to that of a contractor. Employees are typically paid on a periodic basis based on hours worked. Independent contractors are usually paid a pre-negotiated amount upon submission of an invoice at the completion of a service. Further, receipt of a fee as opposed to a regular wage or salary is indicative of an independent contractor relationship.

Wages that are not based on skill, difficulty of task or allotment of time for completion of the job suggest an ordinary employment relationship. Where the worker bears risk for unsatisfactory completion of the job, this suggests a contractor relationship.¹⁹ Payment following submission of an invoice by the worker will also carry weight – unless this has been dictated by the employer.²⁰ In one case, a company generated and issued invoices to itself on behalf of its contractors. The Court examined this process and determined that the recipient-generated invoices were akin to payslips typically issued by an employer to an employee and therefore did not assist a finding that the workers were contractors.²¹ Although the courts do not always consider the mode of remuneration alone as a reliable indicator of the workplace relationship due to contemporary methods of payment, the court has already considered remuneration based on hours of work set out in timesheet entries as one of the (several) factors that indicated an employment relationship²².

Provision of Tools and Equipment

More often than not, where the person has to purchase and maintain his or her own tools and equipment, this will point to a contractor relationship.²³ However, in light of this, modest sums spent on equipment or sums counterbalanced by privileges provided by the employer for the enjoyment of the worker will rarely be significant in the assessment.²⁴

However, owner-drivers again create issues; and it has been found that even where an employer pays for signage on a vehicle owned by a worker, this does not necessarily outweigh the fact that the employee supplies and maintains an expensive piece of equipment.²⁵

To provide contrast, where the couriers, who were responsible for providing and maintaining their own bicycles, were found to be employees, the court noted the relative capital cost of such a burden. Conversely, in another case²⁶, the court found that ownership of a truck is sufficient to satisfy the requirement for investment of capital; and thus held that the owner-driver was a contractor. This was justified by the fact that owning and maintaining a truck is significantly more expensive than a pedal bike.

An independent contractor is likely to make a substantial investment in assets, using their own tools and equipment (for example, their own phone and computer), as well as hold policies of insurance for their business and for public liabilities. By contrast, an

18 Marco Investments Pty Ltd v Amor [2004] SAIRComm 9 at [130]-[139]

19 B D Investments Pty Ltd v Workers Rehabilitation and Compensation Corporation [1994] SASC 4673

20 Marco Investments Pty Ltd v Amor [2004] SAIRComm 9 at [82]

21 ACE Insurance v Trifunovski (2011) 200 FCR 532, [89]

22 Country Metropolitan Agency Contracting Services Pty Ltd v Slater (2003) 124 IR 293

23 Stevens v Brodribb (1986) 160 CLR 16 at 24 per Mason J

24 Yaraka Holdings Pty Ltd v Gilijevic [2006] ACTCA 6 at [43]

25 Australian Air Express v Langford [2005] NSWCA 96 at [44]

26 Australian Air Express Pty Ltd v Langford [2005] NSWCA 96 at [44]

employee would be more likely to use tools and equipment provided to them by their employer and has no obligation to indemnify their employer from loss.

The provision of training in relation to company products and policies can also be indicative of an employment relationship.

Representations to Third Parties

Where a worker is required to don the livery of their employer during their work hours, this will suggest an employment relationship. This was most famously affirmed in a case where a bicycle courier was required to wear a uniform with the company logo “Crisis Couriers” emblazoned on its back.²⁷ Similar examples include providing and directing the worker to use company stationary and a company email address for corresponding with third parties, and the use of the worker’s name or image in marketing materials, in particular, on the company’s website.

Risk and liability

An independent contractor will be responsible for any faults in their work and will often carry their own insurance and indemnify himself. By contrast, an employer will be liable for most of the mistakes of an employee and will have insurance to reflect this.

Business Expenses

An independent contractor is likely to pay their own overheads and business expenses and hold their own policies of insurance and any relevant trading licences, whereas an employee will often be reimbursed by their employer for any costs incurred in the performance of their work.

Exclusive Engagement

The right to the exclusive services of a person is characteristic of an employment relationship. A true independent contractor would be free to perform work for other people.

However, jurisprudence noted that the mere freedom to work for others may be illusory²⁸ – and as such, the court must take into account “*the level of economic dependence of one party upon another, and the manner in which that economic dependence may be exploited*” in applying this test.

Separate Place of Work and Advertises Services

This category is somewhat linked to the above ‘performance of work for others’ test. Put simply, an inference that workers carry on business on their own account is more easily made if they have a location for their own business that is in actuality separate from the impugned employer’s.²⁹

Furthermore, where the worker actively advertises their own business without reference to a connection with their employer, this factor will be in favour of their status as an independent contractor.³⁰

We appreciate that permitting contractors to work for others during the term of their engagement with the Principal may be commercially unwise. Nevertheless, explicit references to the exclusive services of contractors to the Principal, lends weight to an argument for employment. Most Principals allow the contractors to perform work for others, provided that it does not influence their delivery of services to the Principal.

27 Hollis v Vabu Pty Ltd (2001) 207 CLR 21

28 Re Porter; Re Transport Workers Union of Australia at [14] and [26]

29 Stevens v Brodribb (1986) 160 CLR 16, 37

30 Abdalla v Viewdaze [2003] AIRC 504, [35]

Right of Delegation

A requirement that an individual should personally carry out the work is often typical of an employment relationship. Independent contractors frequently have power to delegate work to others, either with or without the consent of the party contracting their services, by either recruiting his or her own employees, or subcontracting the work to others.

The importance of powers of delegation will be touched upon again below. However, the Court of Appeal³¹ held that in deciding whether a person is an employee, it is the totality of the relationship that is important and as such the right to delegate or provide a substitute carried significant weight but was not completely decisive.³² In one case, two insurance salesmen were found to be employees, despite both trading through corporate vehicles and hiring their wives to assist them with administrative tasks.³³

Contractor agreements should contain the express right for the contractor to delegate his work to any other person or entities under the contractor's supervision. Any contractor agreement should ensure that the contractor is solely responsible for ensuring that any agent, employee, contractor or person engaged by the contractor to perform the work complies with all relevant laws.

Employment Obligations and Entitlements (Taxation, Superannuation and Leave)

While the courts have, in the past, considered the treatment of employee entitlements and obligations such as tax deductions, superannuation contributions and leave entitlements as an indication of the workplace relationship, these matters are not determinative.

Typically, an employer withholds applicable tax deductions and superannuation contributions from an employee's remuneration, whereas an independent contractor should be paid a gross (untaxed) amount and is responsible for administering their own taxation and superannuation planning. Further, an employee is entitled to paid leave (such as annual leave, personal leave and parental leave), whereas an independent contractor is not.

At best, the treatment of these obligations and entitlements will assist a court in determining the intention of the parties.

Nature of the Work

In assessing the employment relationship, the level of skill involved in the work may be a factor taken into account by the courts. Independent contractors are typically associated with a provision of skilled labour. Further, unskilled work often implies the need for more control over the worker and therefore, denotes an employment relationship.

Professionals and tradespeople are the two most significant groups that will be considered by a court to be self-employed. A requirement to hold a licence if the person is not considered an employee is only a minor consideration if attempting to deem him or her as a contractor.³⁴

Business Goodwill

A genuine independent contractor will often have the aim to generate its own business goodwill through the services it provides. However, if a worker is expected and/or required by their contracting business to be viewed by the public as a representative of that business (such as through the use of uniforms, business cards and general

representations to the public), the worker's ability to generate business goodwill will be significantly restricted.

The courts will often assess a worker's ability to generate business goodwill independent to their contracting business, in determining whether they are an independent contractor or employee.

Express Label Given to the Relationship

As set out above, the courts' general approach is that they will not necessarily consider themselves bound by the express labels used by the parties but look to the relationship in practice.

However, where the nature of the relationship is ambiguous, consideration will be given to an express label. In this regard, how the parties characterise the relationship and express that in documentation, may be considered by the Courts in determining the intentions of the parties, and as part of the overall factors to be considered. In *Re Porter; Re Transport Workers Union of Australia*, Gray J noted:³⁵

"The parties cannot create something which has every feature of a rooster, but call it a duck and insist that everybody else recognises it as a duck ... [T]here is no particular reason why a court should ignore the practical circumstances, and cling to the theoretical niceties."

The Power to Incorporate

An independent contractor relationship is more likely to be found in circumstances where the contract for service is with a company rather than an individual, as employers do not typically engage companies as employees. In one case however, the Federal Court of Australia determined that the right to incorporate does not preclude a finding that the relationship between the worker and the company was one of employment. Looking into the substance of the relationship, the Court gave little weight to the power to incorporate because *"the entity selected to do the work... was the individual..., and the company featured only as the recipient of the fees that would otherwise have been paid to the [individual]"*³⁶

As has been stated, the primary exception to the above is where the worker is permitted under the employment contract to delegate or subcontract the relevant work without permission or qualification from the employer.³⁷ In these circumstances, the worker will almost always be classified as a contractor.³⁸ However, where that power requires approval by, or conditions to be met to the satisfaction of the employer, this indicator will be given less weight.³⁹

c. General Differences in Tax Treatment

Taxation systems fundamentally differ between employees and contractors. The distinctions can be primarily confined to tax regulation with regards to remuneration of workers; and personal services income provisions for contractors outlined in divisions 83-87 of the Income Tax Assessment Act 1997 (Cth). These will be discussed independently of each other.

Withholding tax from remuneration

In the context of an employer-employee relationship, an employer is obligated under

³¹ Australian Air Express Pty Ltd v Langford [2005] NSWCA 96

³² Ibid., [65]

³³ ACE Insurance v Trifunovski (2011) 200 FCR 532, [95]

³⁴ Abdalla v Viewdaze [2003] AIRC 504, [45]

³⁵ Re Porter; Re Transport Workers Union of Australia (1989) 34 IR 179, 184

³⁶ ACE Insurance v Trifunovski (2011) 200 FCR 532, [95]

³⁷ Queensland Stations Proprietary Ltd v Federal Commissioner of Taxation (1945) 70 CLR 539

³⁸ Ibid.

³⁹ Australian Air Express Pty Ltd v Langford [2005] NSWCA 96; Tobiasen v Reilly [2009] WASCA 26

Schedule 1 of the *Taxation Administration Act 1953* (Cth) to deduct taxes from wages paid to an employee, and remit that sum to the Australian Taxation Office (“ATO”). An employee will be taxed at the maximum rate possible unless they provide their employer with a valid tax file number.⁴⁰

Conversely, the taxable revenue generated by independent contractors is taxed at the applicable company rate, which is ordinarily lower than the tax rates for individual employees. Contractors are also paid the gross sum of earnings and must generally meet their own tax obligations, however, an independent contractor and a business may enter into a voluntary agreement to withhold tax from remuneration payments.⁴¹

Personal Services Income Provisions

A self-employed individual can often claim a much wider range of deductions with regards to their expenses. Given the ease with which a contractor may obtain an Australian Business Number (“ABN”),⁴² engaging as a contractor can be quite attractive to some people, particularly in more senior roles.

The *Income Tax Assessment Act 1997* (Cth), however, places an onus upon individuals seeking to earn income from self-employment to prove that they are genuinely running a ‘personal services business’. Moreover, this requirement will become increasingly pertinent in scenarios where a self-employed individual earns 80% or more of their income from a single source.

The personal services income (“PSI”) test established by the *Income Tax Assessment Act 1997* (Cth) is not dissimilar to the common law test articulated above, however an individual found to be an independent contractor by a court will not necessarily enjoy the same status in light of this legislation.⁴³

The tests include:

- whether they advertise services to the public
- whether they engage others to help perform the work
- whether they have their own business premises
- whether they are paid to produce a particular ‘result’
- whether they are obliged to rectify defects in their work

It is important to note that an employee deemed as such under the PSI provisions does not become an employee for any other legal purpose.

d. Differences in Benefit Entitlements

National Employment Standard

Under the National Employment Standard and the Fair Work Act 2009 (Cth) (**FW Act**), employees are entitled to the following benefits:⁴⁴

- paid annual leave of four weeks;
- maximum working hours of 38 hours per week, plus reasonable additional hours;
- **the ability to request for flexible working arrangements;**
- **parental leave;**
- paid personal leave, including carers and compassionate leave;

⁴⁰ Ibid, 56

⁴¹ See for example, ‘<https://www.ato.gov.au/Business/PAYG-withholding/Payments-you-need-to-withhold-from-Payments-to-contractors-under-a-voluntary-agreement>’ <accessed 12 January 2017>

⁴² Ibid.

⁴³ IRG Technical Services v Deputy Commissioner of Taxation [2007] FCA 1867

⁴⁴ See for example ‘<https://www.ato.gov.au/Business/Super-for-employers/Working-out-if-you-have-to-pay-super/Contractors>’ <accessed 12 January 2016>

- long service leave;
- community service leave;
- public holidays;
- a minimum notice period for termination and a minimum amount of redundancy pay; and
- minimum rates of pay.

In contrast, independent contractors are not entitled to these benefits.⁴⁵

Superannuation

Under superannuation law in Australia, employers have an obligation to pay the superannuation guarantee for their employees at a minimum rate of 9.5% of their base earnings if the employee:⁴⁶

- is paid \$450 or more (before tax) in salary or wages in a month; and
- is 18 years old or over, or
- the employee works for more than 30 hours in a week.

In regards to contractors, a Principal may be obliged to pay superannuation at the minimum rate for a contractor in some circumstances. In particular, if a Principal pays a contractor under a contract that is wholly or principally for labour, the Principal has to pay superannuation contributions for the contractor. This is because the contractor is deemed to be an employee for superannuation guarantee purposes. This is even if the contractor issues invoices under an ABN.⁴⁷

Generally, a contract is principally for labour if more than half of the value of the contract is for the person’s labour, which may include:

- physical labour
- mental effort, or
- artistic effort.⁴⁸

Workers’ Compensation

Workers’ compensation is covered by State and Territory laws and entitles employees to claim benefits for job-related injuries.⁴⁹

Some independent contractors are covered for workers’ compensation in some states and in specific circumstances.

An example is contractors under labour hire services arrangements, who are covered by the NSW workers’ compensation scheme pursuant to the *Workplace Injury Management and Workers Compensation Act 1998* (NSW), which deems them workers for the purpose of claiming workers’ compensation.

However, not all contractors are entitled to claim workers’ compensation and it will depend on the relevant state legislation. All employees however are covered by workers’ compensation legislation and entitled to its benefits.

Benefits under Work, Health and Safety Legislation

Under the various State and Federal Work Health and Safety Acts, a form of which

⁴⁵ Ibid.

⁴⁶ See for example ‘<https://www.ato.gov.au/Calculators-and-tools/Super-guarantee-eligibility/>’ <accessed 12 January 2016>

⁴⁷ See for example ‘<https://www.ato.gov.au/Business/Super-for-employers/Working-out-if-you-have-to-pay-super/Contractors>’ <accessed 12 January 2016>

⁴⁸ Ibid.

⁴⁹ Department of Industry, Innovation and Science, *Independent Contractors: The Essential Handbook* (2016), p.18-19.

applies in all Australian jurisdictions,⁵⁰ a person conducting a business or undertaking must ensure, so far as is reasonably practicable, the health and safety of:

- workers engaged, or caused to be engaged by the person, and
- workers whose activities in carrying out work are influenced or directed by the person,
- while the workers are at work in the business or undertaking.⁵¹

"Worker" is defined broadly under section 7 of the Work, Health and Safety Act 2011 to include both employees and independent contractors.

Accordingly, independent contractors and employees have equal entitlement to a safe and healthy workplace, and both can consequently sue for associated breaches.

e. Differences in Protection from Termination

Termination under Common Law

Under the common law, an employer has the right to dismiss an employee at any time provided that a reasonable period of notice is given.⁵² This is subject to State and Federal laws, as well as to any terms governing termination in the employment contract. In contrast, the relationship between an independent contractor and a Principal is governed by contract. Accordingly, the Principal may only terminate the contract without penalty if the worker has failed to perform its obligations according to the contract terms, by agreement or where the contract provides for termination.⁵³ A breach of contract, resulting in damages, will arise where there is an unlawful termination of the service contract.

Notice Period

Section 117 of the FW Act specifies the minimum period of notice that must be given to an employee or employer on termination of the employment relationship. This period can fluctuate from 1 to 5 weeks depending on the employee's age and length of continuous service with the employer at the end of the day the notice is given.

A contravention of the minimum period of notice may give rise to a cause of action. Conversely, no minimum period of notice is provided under statute for the termination of a contract between an independent contractor and a Principal. As such, protection will only arise if it is provided for in the service contract.

Unfair Dismissal

An employer's common law right to dismiss an employee on reasonable notice is further qualified by the FW Act, which provides statutory protection for eligible employees⁵⁴ from dismissal on grounds that are "harsh, unjust or unreasonable."⁵⁵ Contravention of this provision will result in a remedy being awarded to the employee.

In contrast, independent contractors are not employees for the purposes of the FW Act and therefore cannot access the unfair dismissal regime under the FW Act.

⁵⁰ albeit with some differences between jurisdictions; Victoria and Western Australia in particular have different legislation, though with similar provisions

⁵¹ S. 19 Work, Health and Safety Act 2011 (Cth)

⁵² In the absence of an express provision under statutory instrument or contract, a term of reasonable notice may be implied in contracts of employment; see *Westpac Banking Corporation v Wittenberg* [2016] FCAFC 33, [218]

⁵³ Australian Government, *Independent Contractors: An Overview* (2009), p. 5

⁵⁴ Protected employees are those who have completed a minimum period of service of 6 or 12 months (depending on the size of the company), and whose employment is covered under a workplace award or enterprise agreement, or earn a base salary of less than the high-income threshold, which is presently \$138,900. See s. 382 of the FW Act

⁵⁵ Ss. 365, 385 FW Act, sections 365, 385

Adverse Action

Both employees and independent contractors have rights and remedies pursuant to the General Protections provisions of the FW Act. Those provisions allow both employees and independent contractors to bring a claim if the employer or principal, has taken "adverse action" against them because they have exercised a "workplace right" under a workplace law.

f. Local Limitations on Use of Independent Contractors

The Independent *Contractors Act 2006* (Cth) promotes freedom to enter into genuine independent contracting relationships.

The Act also seeks to minimise limits on the use of independent contractors in genuine contracting relationships.⁵⁶

In particular, the principal objects of the Act are:⁵⁷

- to protect the freedom of independent contractors to enter into service contracts;
- to recognise independent contracting as a legitimate form of work arrangement that is primarily commercial; and
- to prevent interference with the terms of genuine independent contracting arrangements.

Accordingly, there are few limits on the bona fide use of independent contractors.

However, the use of independent contractors will be limited where it is a 'sham arrangement'. Likewise, the law allows a certain level of scrutiny and redress in circumstances where the independent contract is in fact an unfair contract, and makes provision for remedies for unfair contracts.

Moreover, deeming provisions in legislation, such as in superannuation legislation, may impose additional obligations on principals who hire independent contractors.

g. Other Ramifications on Classification

Discrimination Laws

Likewise, whether an individual is classified as an employee or as an independent contractor will not affect their entitlement to seek a remedy under the various state and federal discrimination laws. Employees do, however, have additional protections from unlawful discrimination under the FW Act.⁵⁸

Intellectual Property

The characterisation of a person's employment status may also determine beneficial ownership of intellectual property created by a worker. Copyright in an original work is ordinarily owned by the author of that original work,⁵⁹ however, copyright legislation provides an exception to this rule,⁶⁰ allowing an employer of an author the right to own the copyright subsisting in their original work provided that:

- the worker is engaged under a contract of service; and
- the work was made by the author "in pursuance of the terms of his or her employment."

⁵⁶ Department of Employment and Workplace Relations, Discussion Paper: Proposals for Legislative Reforms in Independent Contracting and Labour Hire Arrangements (2005), p. 9

⁵⁷ Independent Contractors Act 2006 (Cth), section 3

⁵⁸ S. 351 FW Act

⁵⁹ S. 35(2) Copyright Act 1968 (Cth)

⁶⁰ S. 35(6) Copyright Act 1968 (Cth)

The term “*contract of service*” is not defined in the Copyright Act and therefore the courts would apply the common law tests identified above, to determine the existence of an employment or contractor relationship.⁶¹

Negligence

An employer owes a duty of care to his/her employees. Therefore, an employer may be liable for compensation to the employee where there has been a breach of this duty. In regards to the position of independent contractors, the Court of Appeal has held that though a principal owes a duty of care to independent contractors, this duty is not co-extensive with the duty owed by the employer to his/her employees. Similarly, a principal does not owe a duty to control the working systems implemented by the contractor where it is reasonable to assume that the contractors are competent to control their system of work without supervision by the Principal.⁶²

Vicarious liability

An employer is vicariously liable for the actions of his/her employees performed in the course of employment.⁶³

However, an employer is not vicariously liable for any actions committed by an independent contractor in the course of performing work for the employer.⁶⁴

Unfair Contracts

The *Independent Contractors Act 2006 (Cth)* provides independent contractors with a remedy for unfair contracts and it is possible to apply to the court to review and set aside a contract or term under that Act.

Under the *Independent Contractors Act 2006*, an unfair contract is one where a person performs work on terms that are unfair, unconscionable, against the public interest or are designed to avoid the provisions of Federal or State industrial laws.⁶⁵

The *Independent Contractors Act 2006* applies to those who have a service contract with a constitutional corporation, or the Commonwealth, or where a service contract was formed or performed in either the Australian Capital Territory or the Northern Territory.

h. Leased or Seconded Employees

Where a host company enters into a bona fide labour-hire arrangement that is not contrived to disguise what is in fact an employment relationship, the possibility of a court finding the host to be an employer of a worker is still significant, particularly if the work undertaken is permanent and unskilled.

For example, in *Damevski v Guidice*,⁶⁶ a cleaner worked for a firm as an employee. He was then told that he would no longer be employed directly, but would instead be hired through an agency. He signed a document prepared by the firm that indicated his acceptance of an offer of engagement by the agency. However, the firm assured him that “nothing will change”. This helped persuade the court that, viewed objectively, he still had a contract with his original employer and hence could pursue a claim against it for unfair dismissal. This was so even though he was now paid by the agency.

Similarly, the NSW Industrial Relations Commission observed that an agency had no real or effective involvement or control in any aspect of the worker’s recruitment, day-to-

61 University of Western Australia v Gray [2009] FCAFC 116

62 Unilever Australia Limited v Pahi & Anor; Swire Cold Storage Pty Limited v Pahi & Anor [2010] NSWCA 149

63 Hollis v Vabu Pty Ltd (2001) 207 CLR 21; Sweeney v Boylan Nominees Pty Ltd (2006) 227 ALR 46

64 Ibid.

65 S. 9, Independent Contractors Act 2006 (Cth)

66 Damevski v Guidice (2003) 202 ALR 494

day employment and dismissal and held that the agency operated more like a “*service company which was used as a conduit by the Host to pay the applicant’s wages and to deal with on-costs such as workers compensation*”⁶⁷.

It is critical that companies recognise that in any test of characterisation, the substance of any workplace arrangement will prevail over its form. As noted above, the distinction between employers and contractors is “*rooted fundamentally in the difference between a person who serves his employer in his, the employer’s, business, and a person who carries on a trade or business of his own.*”⁶⁸

Labour hire arrangements have recently come under considerable scrutiny by the courts and regulatory bodies, in particular, organisations that engage unskilled and semi-skilled workers through labour hire agencies. The very nature work performed by unskilled and semi-skilled persons lends itself to a finding that the person could not have been running a business of their own and the Courts have described such a proposition as “*prima facie, intuitively unsound*”.⁶⁹ In such cases, the relevant question is not whether the workers were employees or contractors, but whether a contract of employment can be implied between the worker and the labour hire agency, or the worker and the host company in which the labourers work. The host organisations have increasingly been found to be the true employer of the workers so engaged, irrespective of the contractual arrangements in place between the organisation and the labour hire company, and the labour hire company’s contractual arrangements with agents.

In a recent case (“**Quest Case**”),⁷⁰ a company that operated serviced apartments effectively re-engaged two of its long-term housekeeping employees as independent contractors to provide identical housekeeping services, but via a form of tri-partite contracting arrangement, referred to as an “*Odco*” arrangement.⁷¹ Under the Odco contracting arrangement, the workers were first engaged as independent contractors to a third party labour hire company, who in turn, supplied the services of the workers to the Host company under a labour hire agreement.

At first instance, the Federal Court accepted that the Odco arrangement was lawful and therefore held that the housekeepers were legitimate contractors. On appeal, the Federal Court of Australia, Full Court (“*Full Court*”) examined the substance of the housekeepers’ working relationships, applying the multi-factorial totality test and found it improbable on the evidence that any reasonable person would accept that they were working in business for themselves.⁷²

One key point of contention in the Quest Case concerned whether the Host business contravened section 357(1) of the FW Act by misrepresenting to the workers, the nature of their employment relationship with the labour hire business. Section 357(1) provides:

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.

On appeal to the Full Court, the Host company was successful in arguing that section

67 Oanh Nguyen and Thiess Services Pty Ltd (2003) NSWIRComm 1006, [77]

68 Marshall v Whittaker’s Building Supply Company (1963) 109 CLR 210, 217 per Windeyer J; cited with approval in Hollis v Vabu Pty Ltd (2001) 207 CLR 21, 39; ACE Insurance v Trifunovski (2011) 200 FCR 532, 543

69 Hollis v Vabu Pty Ltd (2001) 207 CLR 21, [48]; Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] FCAFC 37, [183]

70 Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] FCAFC 37; Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] HCA 45

71 From the case of Re Builders Workers’ Industrial Union of Australia; William Oliver; Jo McPartlin; Victorian State Building Trades Union; Hugh Harkins and Martin Bingham v Odco Pty Ltd [1991] FCA 87

72 Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] FCAFC 37, [191]

357(1) had limited application and could not extend to representations made by an employer to an employee, to the effect that the employee was engaged under a contract for services with a third party.⁷³ In finding that the workers were employees of the Host, but that the Host had not contravened section 357(1), the Full Court left a loophole that would protect Host businesses, utilising Odco contracting arrangements, from liability to pay pecuniary penalties for contravening the Sham Contracting provisions of the FW Act.⁷⁴

However, on a subsequent appeal to the High Court of Australia, that decision was overturned. The High Court held:⁷⁵

The prohibition in s 357(1) is against an employer making a particular representation to an employee or prospective employee. The prohibited representation concerns the character of the contract, which exists or would exist between the employer and the employee as a contract of employment, under which the employee performs or would perform work. The content of the prohibited representation is that the contract of employment is or would be a contract for services under which the employee performs or would perform work as an independent contractor.

The cumulative decisions of the Full Court and the High Court in the Quest Case have effectively neutered the use of Odco style contracting arrangements as a means of circumventing the Sham Contracting Provisions of the FW Act. The Quest Case has now been returned to the Federal Court to determine pecuniary penalties.

Genuine labour hire arrangements are, nevertheless, still commonplace in Australia, particularly for casual staff, short-term projects and transient workers, such as seasonal labourers. Secondments are also common, particularly for skilled technicians and workers in professional services fields, such as accounting, law and medicine.

Tortious Liability

On a separate note, a worker under a labour hire agreement ("Agency Worker") may cause damage either to the host or to a third party whilst working under the labour hire agreement. While an employer is vicariously liable for the tortious wrongdoings of an employee during the course of employment, there are additional complications for host businesses.

The key principle is that if the host has assumed effective control over all facets of the Agency Worker's work so that the agency worker becomes the temporary employee of the Host, then the host, instead of the agency, can be liable for the tortious conduct of the Agency Worker if injury is caused to a third party.

In the Victorian case of *Deutz Pty Ltd v Skilled Engineering*,⁷⁶ a labour hire company hired out a forklift driver, who, whilst driving the forklift, negligently caused extensive damage to the host's property. The court was reluctant to conclude that there had been a temporary transfer of employment from the labour hire company to the Host based on the following principles:

- only in exceptional circumstances will an Agency be able to shift vicarious liability to a temporary employer (i.e. host);
- transfer will be less readily inferred when a worker is hired out with a machine or where a skilled worker is provided;

⁷³ Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] FCAFC 37, [239]-[240]

⁷⁴ Part 3-1, ss. 357-359 Fair Work Act 2009 (Cth)

⁷⁵ Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd [2015] HCA 45, [14]

⁷⁶ Deutz Pty Ltd v Skilled Engineering [2001] VSC 194

- transfer may occur where the Agency Worker is operating the equipment under the absolute control of the Host; and
- a transfer may occur in certain circumstances, including where the Host can direct not only what the workman can do, but how he is to do it.

The Court held that there had been no temporary transfer of employment to the host, rather the agency retained control. The agency had recruited the worker, paid his wages, established safety protocols, provided safety training, provided clothing with the agency logo, supervised the worker and had the power of dismissal.

Therefore, if labour hire mechanisms are implemented, it is important that the host genuinely sever the relationship of control between it and the worker in order to reduce its exposure to a claim in tort.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As outlined above, the existence of an employment relationship is a question of fact, not law, and is circumstantial in nature. As such, in the absence of a substantive change in the nature of the work performed, 're-characterisation' is procedural, providing redress to interested parties for any loss arising from misclassification.

In circumstances where a genuine independent contractor is engaged by its Principal under a contract of employment, it is assumed that there will have been a fundamental change in the terms of engagement between the parties. In those circumstances, the company's duties and obligations with respect to that employee will be the same as its duties and obligations in relation to any other employee. In addition, any period of service to the company by an independent contractor does not count as continuance service for the purposes of the FW Act, limiting the newly engaged employee's access to accrued paid leave (annual, personal, parental and long service leave), and affecting the employee's entitlement to notice on termination and redundancy entitlements.⁷⁷

Companies wishing to re-engage contractors as employees should take care to document their reasons for changing the employment status of the worker, as well as keeping records of any discussions and agreements reached between the company and the putative employee. It is also recommended that the company identify in writing, any characteristics of the new position that distinguish it from the role that the person previously performed as an independent contractor.

b. The Legal Consequences of Re-Characterisation

Financial Consequences

The risks and consequences of unlawfully engaging workers as independent contractors, in circumstances where the true substance of the working relationship is an employment relationship, can be devastating to a business.

The main source of legal exposure arising out of a situation where a business engages the workers as independent contractors in circumstances where the workers are in fact employees is in respect to unpaid employee entitlements (potentially leading to significant claims for back-pay) and liability in respect to non-compliance with statutory obligations. These potential liabilities are detailed as follows:

i. The workers would be entitled to receive unpaid statutory benefits and award

⁷⁷ Ss. 117 and 119, FW Act

entitlements, plus interest⁷⁸, backdated to the date their contract of employment is deemed to have commenced.⁷⁹ Such benefits include paid leave, their base salary as prescribed under an industrial award⁸⁰, any allowances provided under an award, such as payments for overtime or reimbursements, payment for public holidays and superannuation payments;

ii. The employer may be liable for penalties of up to \$54,000 per contravention of the civil remedy provisions of the FW Act, which include:

- failing to provide employment entitlements under an industrial award;
- failing to provide paid leave in accordance with the National Employment Standards of the FW Act;
- failing to maintain proper employment records;
- failing to withhold PAYG tax;
- failing to pay superannuation; and
- misrepresentation in relation to the use of sham contracting arrangements.

iii. The company may be penalised for having failed to hold complying policies of insurance for Workers Compensation⁸¹ and would be required to pay backdated workers compensation premiums;

iv. Large companies with a monthly payroll of \$750,000 or more could be liable to State taxation offices and could be required to pay penalty tax⁸² for default on any payroll tax payments;

v. The company may also face significant penalties from the Australian Taxation Office, including penalty interest, for non-payment of superannuation⁸³ and non-compliance with PAYG withholding and reporting obligations;⁸⁴

vi. A company may also suffer considerable damage to their reputation, if it is found to have been a party to a sham contractual relationship intended to avoid liabilities associated with employment.⁸⁵

Unfair Dismissal and General Protections

A worker may be able to access the unfair dismissal provisions of the FW Act on the basis that she was actually an employee.

Under the FW Act, a worker is not permitted to access the unfair dismissal jurisdiction unless he or she has worked the “minimum employment period” specified in the legislation. The minimum employment period is a period of 6 months. If a worker is found to be an employee, and his or her total earnings are less than the prescribed remuneration

⁷⁸ Simple interest on unpaid employment entitlements can be claimed in legal proceedings at the ‘pre-judgment’ rate, which is four basis points above the cash rate target set by the Reserve Bank of Australia. The current pre-judgment interest rate is 5.5% and will be reviewed on 1 July 2017.

⁷⁹ Statutes of limitations apply in both Federal and State jurisdictions, limiting claims for payment of monies owed under a contract to 6 years from the date the contract is purported to have been breached. See for example s. 14, Limitations Act 1969 (NSW).

⁸⁰ Where a contractor’s remuneration can not be determined in advance, such as with commission payments and performance bonuses, the money they received will not be reclassified as wages for the purpose of the FW Act. In the event of a claim for underpayment of wages, the company will not be able to rely on the fact that they paid commissions to the employee. Commission only remuneration structures are generally unlawful in Australia.

⁸¹ See for example section 155(1) of the Workers Compensation Act 1987; the current maximum penalty in NSW is 500 penalty units (\$55,000) and/or 6 months’ imprisonment.

⁸² Currently 10.8% interest in New South Wales. See for example <http://www.osr.nsw.gov.au/taxes/payroll> <accessed 12 January 2017>

⁸³ fixed 10% interest on unpaid amount plus \$20 admin fee per quarter.

⁸⁴ Roy Morgan Research v Commissioner of Taxation [2010] FCAFC 52

⁸⁵ Office of the Fair Work Ombudsman, June 2015: A report on the Fair Work Ombudsman’s Inquiry into the labour procurement arrangements of the Baiada Group in New South Wales

cap (currently \$138,800), the worker may seek reinstatement or compensation of up to six months’ remuneration.

Similarly, a claim could be made under the general protection provisions in the FW Act, which prevents employers from taking “adverse action” against an employee for their exercise of a workplace right in accordance with a workplace law.

As noted above, the general protection provisions of the FW Act are also specifically available to independent contractors.

Penalties Under the Sham Contracting Arrangement Provisions of the FW Act

The sham arrangements provisions contained in the FW Act impose penalties on employers who misclassify employees as independent contractors. Employers must not:

- misrepresent an employment relationship as an independent contracting relationship – that is, by representing to a person who is actually an employee that they are an independent contractor; or
- dismiss or threaten to dismiss an employee in order to engage the employee as an independent contractor to perform the same, or substantially the same, work.

If an employer makes representations to workers that they are independent contractors in circumstances where they are employees, the company could be liable for a penalty of up to \$54,000 and \$10,800 per occasion for any individual involved in the contravention (such as a director or relevant manager).

In 2013, an airport shuttle bus service company and its managing director were fined a total of AUD\$295,000 for engaging seven of its drivers as independent contractors.⁸⁶ The penalties imposed included penalties for misrepresenting employment contracts as independent contractor arrangements and for failing to meet award entitlements. The penalties imposed were in addition to the employment entitlement underpayments owed to the individual drivers. The Fair Work Ombudsman initially identified the breaches after the business was selected for auditing in April 2011.

The FW Act does provide a defence to the sham contracting provisions. An employer will not have engaged in sham contracting if the employer did not know about the independent contractor relationship and was not reckless to the fact that the workers were employees rather than independent contractors. However, the burden of proof in relation to this defence rests with the employer.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

A person engaged as an independent contractor may seek a declaration that they are or were an employee from the Fair Work Commission or from any Court or Tribunal exercising common law jurisdiction. Underpayment and sham contracting cases typically involve persons seeking declarations covering the period of their engagement. Where a person is successful in obtaining declaratory relief, the person may then seek an award of damages from a State or Federal Court in respect of any forfeited entitlements that would otherwise have accrued during the course of their employment.

Individuals can also lodge a complaint with the Fair Work Ombudsman, which is a Federal statutory body that functions as both advocate and umpire in relation to compliance with workplace laws. The Fair Work Ombudsman will ordinarily investigate claims of sham contracting in response to a complaint received by a worker, however, the Ombudsman is empowered to investigate and commence civil proceedings against a company of its own volition (that is, without the workers’ involvement).

⁸⁶ Fair Work Ombudsman v Happy Cabby Pty Ltd & Anor [2013] FCCA 397

The Australian Taxation Office is also similarly empowered to investigate and determine an individual's taxation liabilities and superannuation entitlements of its own volition. In such circumstances, the ATO may disregard the form of contracts between the parties and assess their respective tax liabilities on the basis that the relationship is one of employment. The ATO does not, however, have the power to bring civil claims on behalf of employees in relation to employment entitlements generally.

Independent contractors should also be mindful that in the event they are deemed to be employees, they may suffer a detriment if they are reassessed by the ATO and ordered to pay the difference between the company tax rate they already paid, and the individual tax rate they should have paid. This can be further compounded where a contractor's gross income is readjusted to include amounts previously deducted or offset under relevant company tax provisions.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Prior to engaging an independent contractor, a company should first consider whether the work can properly be the subject of a contract of employment. It is unlikely that some types of work would ever be considered as independent contractor work, such as a receptionist, factory worker and clerical employee. At the other end of the spectrum, the fiduciary duties owed by senior executives to their employer companies may also preclude the possibility of their being engaged as independent contractors.

If the work is suitable for being performed by a contractor, it is important to ensure that the parties enter into a properly drafted independent contractor agreement, which sets out the rights and obligations of each party. The contract should make clear that the relationship is that of an independent contractor and principal, and clearly set out rights and duties consistent with a contractor-principal relationship, including (where appropriate):

- i. That the principal does not have an inherent right to control the manner in which the work is performed;
- ii. The work should be identified by reference to a specific task or tasks;
- iii. The contract should avoid seeking to establish fixed hours of work;
- iv. The contract should not be open-ended, but rather it should have a fixed term of operation;
- v. The contract should be entered into between the principal company and the trading entity operated by the independent contractor and should not require that the work be performed only by the contractor;
- vi. The contractor should be required to maintain their own licences and policies of insurance for public liability and workers' compensation. It is recommended that companies also include a term in the contract that the contractor must provide certificates of currency for all relevant insurances and licences;
- vii. Payment under the contract should be linked to the completion of tasks rather than by reference to the number of hours or days worked;
- viii. Contractors should be required to prepare and submit their own invoices for payment;

ix. Where it is expected or anticipated that a contractor will create a product or work capable of being traded for value, the contract should clearly state whether that work is to be assigned to the principal company and include an acknowledgement by the contractor that their payment received under the contract is sufficient valuable consideration for any work created by them in performance of the contract;

x. Further, contracts of employment imply a term of confidentiality, so it is necessary for the protection of the business to ensure that the contractor agrees to protect the confidential information of the principal company.

Ideally, the independent contractor should be an incorporated entity with an Australian Business Number, which itself employs an employee to perform the services. In circumstances where the principal contracts with an independent contractor, which is a company, it is far more difficult for a court to find that the individual actually doing the work is an employee of the principal.

In addition, the fees payable to the contractor should at least be equivalent to the base remuneration that the contractor might have received if they performed the same work as an employee. In the event of an adverse finding of sham contracting, evidence that the contractor had been remunerated at or above minimum wages can mitigate against a claim that the worker suffered a disadvantage an independent contractor relationship in order to have a clear and enforceable understanding of the rights and obligations between the parties.

b. Day-to-Day Management of the Relationship

A well-drafted contract will not be sufficient to protect a company from an adverse finding of sham contracting. The substance of the relationship, as evidenced by its day-to-day nature, must also be maintained. The principal should therefore ensure that its managers manage the relationship with the independent contractor in a manner that is consistent with its independent nature, rather than in the same manner and with the same expectations that the Principal may have of its own employees.

It is important to prepare for the possibility that the nature or characterisation of a relationship may be questioned. In keeping this in mind it may be useful to keep a record of any information that supports a verbal contract or the interpretation of a written contract, this may include; email communications, notes from meetings, quotes from conversations, diary entries, lists of specifications and any form of reporting or tasks lists.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Sham contracting arrangements can be exploitative when created by the principal company purely for the purpose of avoidance of tax and liability for employment entitlements. Further, under section 550 of the FW Act, persons involved in contraventions of the FW Act may be found liable for contraventions of the FW Act, irrespective of their contractual relationship with a worker. Section 550 provides:

- 1) A person who is involved in a contravention of a civil remedy provision is taken to have contravened that provision.
- 2) A person is involved in a contravention of a civil remedy provision if, and only if, the person:

- a) *has aided, abetted, counselled or procured the contravention; or*
- b) *has induced the contravention, whether by threats or promises or otherwise; or*
- c) *has been in any way, by act or omission, directly or indirectly, knowingly concerned in or party to the contravention; or*
- d) *has conspired with others to effect the contravention.*

The Fair Work Ombudsman has increasingly relied on section 550 claims to pursue penalties against individual directors and managers, as well as entities within the supply chain.

The Fair Work Ombudsman, Natalie James, stated at a recent convention:⁸⁷

“The accessorial liability provisions have been well utilised by the Fair Work Ombudsman. Ninety-two per cent of matters my agency filed in court last financial year took action against an alleged accessory.

And accessories don’t just include company directors, or advisers. We’ve also joined other companies in the supply chain – companies that contracted or outsourced to the employing entity, and should have known workers’ entitlements were not being met.

...

What we find in practice, within supply chains and networks like franchising systems, is that there is often someone at the top or the centre of the network who – while not the employer – controls key settings, including how much money is being paid down the line. It is our standard practice to ask who is the ultimate beneficiary of exploited labour and what role have they played in what has occurred.”

A recent investigation conducted by the Fair Work Ombudsman into the operations of Baiada Group⁸⁸, which are a large poultry supply company, found that Baiada Group were using multi-layered system of contractors to perform predominantly manual labour. The complex system of contractors and sub-contractors used ensured that the host organisation had very little control over the way its workers were paid, however it retained absolute control over the manner in which they worked. In its report, the Ombudsman determined that the workers, who were mostly migrants with little to no knowledge of Australian employment protections, had been inappropriately classified by Baiada as independent contractors.

The Baiada investigation is one of many investigations into sham contracting that has looked beyond the contractor/principal relationship to trace the entire supply chain in order to identify parties involved in contraventions of the FW Act. Acting Fair Work Ombudsman, Michael Campbell was recently quoted as saying “[t]he desired end result is that all parties in the supply chain recognise and accept their social, moral and corporateresponsibility to ensure compliance with workplace laws.”⁸⁹

The Baiada investigation also follows on from the Quest Case, in which the High Court all but closed the door on the use of tripartite contracting relationships, or “Odco” model arrangements.

b. Recent Amendments to the Law

There have not been any recent significant legislative changes in relation to the characterisation of employees and contractors. However, one piece of proposed legislative reform is a bill that is currently before the Senate; the Fair Work Amendment (Protecting Australian Workers) Bill 2016 (**the Bill**). The Bill, if passed, will introduce a ‘reasonable person’ element to the test as to whether a person is an employee or an independent contractor. The Bill is also slated to include provisions that will ensure foreign workers on working visas better access to the same protections and entitlements as permanent residents, and, will also increase the powers of a Court to impose penalties against individuals that operate phoenix businesses structures.

VI. CONCLUSION

The Fair Work Ombudsman and the Courts have taken hard line approach to sham contracting in recent years due to systemic exploitation of workers by businesses across multiple industries, in particular, hospitality and tourism, manufacturing, agriculture and marketing. In most of these cases, the workers have been unsophisticated, unskilled, or semi-skilled labourers with little to no business knowledge. In such cases, the Courts have held that it is highly improbable that work being performed by labourers could

support a finding that they were conducting a business for themselves. So on the other hand, individuals working in positions requiring specialist skills and qualifications, and properly engaged to perform specific tasks for a fee, are far more likely to be held to be independent contractors.

Despite the recent trends in Australia, businesses should still consider using independent contractors as an option due to the flexibility and potential labour costs savings, particularly in the long term. However, businesses need to be mindful that it is not possible to eliminate all risk of an adverse finding of sham contracting and therefore they should seek legal advice before engaging staff as independent contractors.

The most important issue to consider when engaging independent contractors in Australia, is that the substance of the contracting relationship must reflect the character of a business relationship, and so the written contract, and day-to-day management of the relationship, must be structured accordingly.

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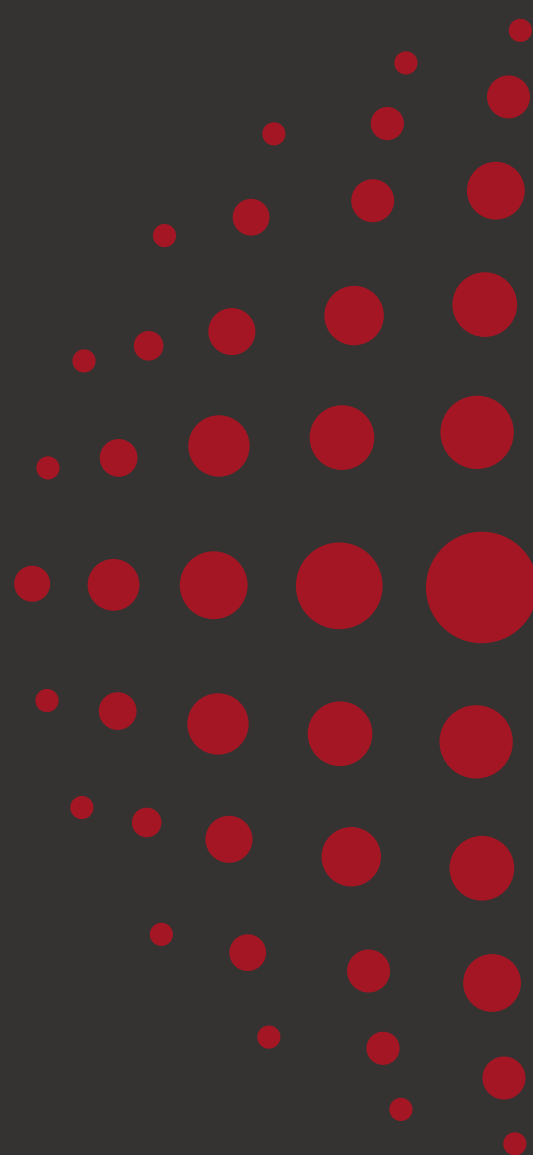
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⁸⁷ Natalie James, Fair Work Ombudsman (10 October 2016): “Getting ahead of the curve on franchise regulation”, Opening remarks - Keynote Panel Session, National Franchise Convention 2016.

⁸⁸ Office of the Fair Work Ombudsman, June 2015: A report on the Fair Work Ombudsman’s Inquiry into the labour procurement arrangements of the Baiada Group in New South Wales

⁸⁹ Media Release - Fair Work Australia (6 October 2016): Australian charities face scrutiny in new Inquiry <https://www.fairwork.gov.au/about-us/news-and-media-releases/2016-media-releases/october-2016/20161006-charity-inquiry-mondial-release> <accessed 13 January 2017>



AUSTRIA

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I. OVERVIEW

a. Introduction

Since every activity or project arising from an employer-employee relationship can also be the subject of an independent service contract, the question of whether a true economic relationship is best described as an employment contract or as an independent service contract can only be judged in individual cases and according to the true economic content of that relationship. Independent contractors have reduced protection under labour law. For example, independent contractors are entitled neither to collective bargaining agreement wages nor (unless otherwise agreed between the employer and the independent contractor) to special payments or paid holidays.

As independent contractors are treated like self-employed people for tax purposes, they are subject to income tax, but not to earnings tax. They are liable for the payment of the income tax. The income tax liability is settled by the contractor's annual taxable income. If his or her income exceeds the sum of 11.000 Euro, he or she must pay tax for them.

A re-characterization (changing the status of a contractor into an employee) is not made automatically but can be done by Court decision. However, the Austrian government's intended project for 2017 is to create an external authority to check hidden employment relationships on a case-by-case basis.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Under the current Austrian labor law regime, the determination of whether an individual is a standard employee or an independent contractor hinges on their personal and economic dependence upon the employer. Austrian employment law provides many protections for the rights of employees. However, these protections are subject to numerous exceptions depending on the specific classification of the employee.

Austrian employment relationships still operate with an antiquated distinction between white collar and blue collar workers. This distinction provides different protections to separately classified employees. Blue collar workers refers to those employees who perform predominantly manual labor and white collar workers refers to those who perform non-manual labor. Due to the basic disparity in power relations between an employer and a blue collar worker, Austrian statutes confer substantial protections to blue collar workers and lessened protections to their white collar colleagues. The distinction between full-time employees and an independent contractor (whether blue or white collar) is based on the level to which the employee operates under the professional purview of the employer. The typical employment arrangement entails an employee working directly under the employer's control, on the employer's premises, and using the employer's resources to carry out their assigned tasks. Another cornerstone of the typical employment arrangement is the employee's economic dependence upon the employer for their livelihood. Typical employment arrangements, like service contracts or freelance labor, do not have these same characteristics, and therefore fall under a different set of laws and regulations.

The current body of Austrian labor law allows for different kinds of independent contractor arrangements that confer varying degrees of protections and benefit entitlements to contractors and employers. The two most prominent legal forms of non-standard employment arrangements are Service Agreements (*Freier Dienstvertrag*)

and Agreement for Work and Services (*Werkvertrag*). Within the scope of the Service Agreement, an employer agrees to hire an employee to provide limited services for a definite period. However, the affected employee is not as fully integrated into the employer's organizational chain or as dependent upon the employment for their continued livelihood as a typical employee. Furthermore, the contracted employees generally use their own resources to carry out the contracted tasks and do not generally guarantee the success or sufficient quality of the agreed services. This service agreement usually covers either students or pensioners who work part time, providing only a limited number of hours per week.

There are differences in legal substance between the *freier Dienstvertrag*, the *Werkvertrag*, on the one hand and the *Dienstvertrag* on the other hand. Employment may be defined as *Dienstvertrag* if the employment relationship entails a majority of the following factors:

- an ongoing employment relationship,
- the employee's relative independence from the employer for continued livelihood,
- a lack of binding organizational directives such as an employee handbook,
- the contractor is free of restrictions upon personal behavior,
- the employee's ability to regulate some facets of their own work product,
- the employer only need provide the essential operating resources, while the employee contributes their own tools to complete the contracted task,
- the contractor has no obligation to perform the work or service personally, and may sub-contract the assigned project.

b. General Differences in Tax Treatment

Generally, Austria has a progressive income tax structure that applies tax rates that range from zero to fifty percent depending on the competent regional authority's end-of-year taxable income assessment. Employers deduct their employees' income tax at the source and redirect it to the competent government authority. This monthly deduction is counted against the employee's annual income tax liability, which is eventually balanced at the yearly tax assessment, taking into account the employee's full income declaration. The Austrian Income Tax Act (*Einkommensteuergesetz*) lists specific types of income that fall under its purview. These mentioned types of income include income from agriculture, self-employed work, tradecraft, standard employment, capital gains, and from real estate.

Within this tax structure, if an employee is classified as an independent contractor, then they will be treated as if they are self-employed persons. With this classification, they are subject to standard income tax, but remain exempt from earnings tax. As stated earlier, they must settle their income tax payment in accordance with their annual taxable income (less deduction). The minimum income threshold that activates Austrian income tax in this setting is € 11.000.

c. Differences in Benefit Entitlement

Austria implements a strong social security system that requires employers to direct both their employee's social security payments and the employers' portion to the Regional Health Insurance Fund. Within Austria's social security system, employees make contributions based on their income. Employee contributions generally amount to approximately 18% of their calculated gross income. Minutely different rates apply to blue and white collar workers. These contributions are capped at €4.980 per month for normal remuneration, and €9.960 per year for special payments. Furthermore, low income employees are exempt from making contributions to the system, the threshold for this exemption being €425,70. Since 01.01.2017 there is no daily threshold for this

exemption anymore. In addition to employee contributions, employers make similar contributions to the social security system - paying approximately 22% of their employee's gross income.

Independent contractors who have a monthly income lower than the minimum threshold that would trigger mandatory social security contributions still require a certain degree of insurance. If an employer agrees to enter into a service contract with this independent contractor, they must enroll the contractor in an accident insurance institution before the commencement of employment. Additionally, the independent contractor whose income falls below the minimum threshold may enroll directly for supplementary health and pension insurance.

If the independent contractors' monthly salary exceeds the minimum threshold listed above, they are required to register as independent contractors with the Regional Health Insurance Fund. Once they complete this registration, they are covered by standard Austrian social security protections – including accident, health, and pension insurance. Furthermore, Austria has recently enacted legislation that requires independent contractors who have a monthly salary above the minimum threshold to sign up for unemployment and bankruptcy insurance on a voluntary base, which in turn entitles them to unemployment entitlements if the well runs dry and they cannot maintain consistent contracted employment.

Independent contractors' social security benefit entitlements mainly differ from standard employees' in that the employer's insurance obligation to draw the employee's monthly contributions as well as make their own contributions to the social security fund cease once the contracted employment relationship ends. The end of the employment contract, and therefore the employer's obligation, legally ends once the independent contractor no longer has a claim for remuneration.

d. Differences in Protection from Termination

According to the Austrian General Civil Code (*Allgemeines Bürgerliches Gesetzbuch*) independent contractors do not enjoy the same level of protection as normal employees. However, in the realm of protection from termination, the same provisions that apply to standard employees apply to independent contractors. Therefore, the same procedures of notice or exceptions to the requirement of notice that bind employers in standard employment arrangements, similarly bind employers when seeking to terminate independent contractors. Independent contractors cannot challenge the termination for being socially unfair. Furthermore, independent contractors cannot take legal action against any notice given on unlawful grounds. In order to establish the independent contractor's employment with a given employer they need not have a written contract, although it is preferable to have one. If the employer does not create an employment contract, then they are at the very least required to hand out a service note to any contractor insured under Austria's General Social Insurance. This note should include a general summary of the services contracted.

However, independent contractor's rights fall short of those guaranteed to standard employee's rights regarding post-termination remuneration. Since independent contractors are not protected by the provisions of the Salaried Employees Act, they are not qualified for entitlement of accumulated vacation days, and continued remuneration based on severance. Further, during the period of their employment, they are not protected under the other various rights conferred by the Salaried Employees Act, including the Working Hours Act, and the Act on Rest Periods.

e. Local Limitations on Use of Independent Contractors

As already mentioned every activity or project arising from an employer-employee relationship can also be the subject of an independent service contract. There are only a few branches with limitations on use of independent contractors, like in the federal public sector. Furthermore, an apprenticeship is a special employment contract and by law cannot be concluded with independent contract.

f. Other Ramifications of Classification

Generally, Austrian courts and Austrian law heavily lean towards protecting employee rights, as the foundation of Austrian labor law is the presumption that the employer holds the upper hand in negotiations with its employees. One specific ramification of this tendency is especially apparent in the scenario of hiring foreign workers within Austria. Employers are free to have a choice of law when hiring foreign citizens legally residing and working within Austria. Therefore, the employer in this scenario may choose to apply the foreign law to this specific employment agreement. However, taking into consideration Austria's tendency to protect employees, if the employee challenges that employment agreement as unfavorable, especially when compared to the minimum standards of relevant Austrian employment law, the courts may still find that Austrian law will overrule the disadvantageous foreign employment law terms and disregard any pre-existing contract that the parties signed.

g. Leased or Seconded Employees

In Austria an employee leasing agency is obligated to have a business license in accordance to the provisions of the Trade, Commerce and Industry Regulation. Basically, since leased employees are not excluded from the scope of mandatory provisions under employment law, all these provisions apply to leased employees as well as to non-leased employees. Additionally, the Temporary Work Act (*Arbeitskräfteüberlassungsgesetz*) includes further provisions concerning minimum legal standards.

In case of a **secondment** from an EU- or EEA country or Switzerland the secondment has to be notified electronically to the ZKO one week prior the commencement of work in Austria. The foreign employer has to keep a copy of the residence and work permits or certificates as well as the employee's social security document (A1 or E101) available at the place of work for the whole duration of the secondment. The authority can impose fines in case of infringements of these obligations. For secondments from other countries, a secondment permit or an employment permit are required under the Employment of Foreign Nationals Act (*Ausländerbeschäftigungsgesetz - AuslBG*).

However, to protect temporary workers from discrimination compared with regular employees in recent years several individual acts were created, for instance the Temporary Work Act (*Arbeitskräfteüberlassungsgesetz*) or the Employee Protection Act (*Arbeitnehmerschutzgesetz*).

h. Regulations of the Different Categories of Contracts

In the absence of a specific agreement between an employer and an independent contractor, the regulations of the Salaried Employees Act (*Angestelltengesetz*), the vacation law, the Working Hours Act (*Arbeitszeitgesetz*), the Act on Rest Periods (*Arbeitsruhegesetz*) and the Continued Remuneration Act (*Entgeltfortzahlungsgesetz*) do not apply to independent contractors. Their legal relationship is only determined by the Austrian General Civil Code (*Allgemeines Bürgerliches Gesetzbuch - ABGB*). Nevertheless, contractors are also involved in the system of pension funds for staff and the self-employed (*Mitarbeiter- und Selbständigenvorsorgegesetz - BMSVG*).

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Employment laws in Austria dictate that the nature of the employment relationship will govern whether that relationship is legally defined as a standard employment relationship, and incur all of the entitlements and protections of Austrian labor law, or whether that relationship is a freelance, service agreement, or independent contract agreement. At the outset of any employment agreement, the employee should obtain a written contract of employment. However, although an employee should obtain a written contract in case there is any labor dispute during their period of employment, an employment contract is not necessary. A contract of employment may be constructed verbally or implicitly and still be legally enforceable.

Within the scope of re-characterization of independent contractors, an independent contractor may claim that their employment agreement exceeds that of an independent contractor. The decisive basis for this assessment is the manner in which the employee's services are effectively carried out on a day-to-day basis, notwithstanding the terms of the employment contract or even the intention of the two parties at the time of the creation of the employment agreement. The decisive factors that define a standard employee as opposed to an independent contractor are:

- personal dependency
- economic dependency
- continuous obligation
- obligation to work for a certain period of time
- use of the employer's equipment
- incorporation into the employer's organization
- success of the assigned tasks directly benefits the employer
- the employer incurs the risk of production

While all of these factors are not required to be present, if the majority of these characteristics outweigh the characteristics of an independent contractor, then the competent authority will find that the employment arrangement was, in fact, a standard employment contract as opposed to an independent contract.

A parallel example of the dangers of a re-characterization of an employment agreement can be found in the re-characterization of a fixed term contract to an indefinite employment contract. Employers in Austria are permitted to create fixed term contracts with their employees that come to a natural conclusion at the end of the fixed term. However, if an employer engages an employee in consecutive fixed-term contracts and the employee can claim the many characteristics of an indefinite employment contract listed above, then, as long as the employer does not have a special social or economic reason for the consecutive fixed-term contracts, the employee may claim all of the benefits of an indefinite employment contract. In the same sense, if an employee who started out as an independent contractor starts to take on the characteristics of a standard employee, they may have a claim for a re-characterization of their employment. The legal consequence of a re-characterization of an employment relationship would be that the former contractor would become entitled to all of the related protections and entitlements, which are extensive, and much more expansive than those granted to an independent contractor.

b. The Legal Consequences of a Re-Characterisation

In case of re-characterization, the employer would be liable for the income tax and the

social insurance contributions that should have been deducted. Concerning the contributions for the social insurance, additional costs may arise as a result of the delayed payment. Moreover, the former independent contractor may be entitled to higher wages following the respective collective agreement. In this case, the employer is obliged to pay the remaining amount. Finally, the former independent contractor becomes entitled to all of the related protections and entitlements, which are generally extensive, and much more expansive than those granted to an independent contractor.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

All Austrian employees are automatically members of the Chamber of Labor. The Chamber of Labor as well as organization-specific works councils and industry-specific trade unions represent employees' varied interests and are independent democratic institutions. Membership in the Chamber of Labor has the benefit of providing employees with legal representation, if necessary. Therefore, as an initial measure, an employee seeking a re-characterization of their employment agreement may petition the Chamber of Labor for legal representation. Subsequently, the employee may bring their case directly to their organizations' employee works council and their employer. If the employee works council cannot resolve the re-characterization of employment claim with the employer, then the petitioning employee may bring their claim to the competent labor court of first instance. These labor courts have jurisdiction over disputes concerning employment related contracts, and may submit a conclusive judicial holding on whether or not the employee is entitled to the claimed re-characterization.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In the event of re-characterization of an Agreement for Work and Services the employer has to pay fees and social security contributions with retroactive effect. Moreover, the authorities can impose several fines: The financial police will impose a fine between €730 and (max) €2.180 per employee working without any valid declaration. In case of recurrence the fine will increase between €2.180 and €5.000. The competent social insurance agency will charge a cost contribution of €800 for the procedure itself and €500 per employee without any valid declaration. In Austria these administrative penalties were steadily increased in recent years.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

As stated above, an independent contractor relationship does not require a written contract. However, to clearly define an employment relationship from the outset, an employer is generally obliged to provide the contractor with a written statement of terms and conditions (*Dienstzettel*). This statement must include basic information regarding the employment arrangement, including, at a minimum, the following elements:

- the names of the two parties,
- basic salary or wages,
- the nature of the proposed work,
- date on which the arrangement commences,
- duration of the notice period,
- any classification within the labor system.

If the independent contractor is supposed to work abroad for more than one month, the

statement of terms and conditions must additionally include information about:

- the expected duration of the foreign operations,
- the currency in which salary or wages are to be paid,
- the conditions of the return to Austria and
- potential additional payments.

This written statement of terms and conditions is often required by the employee to register for social insurance, if they are seeking to do so independent from their employer. The employer is obliged to issue the statement in written form immediately following the start of the independent contractor relationship, at the latest however, within one month. In case of changes concerning the information included in the statement, the employer is obliged to give immediate notice to the independent contractor in writing. However, a statement of terms and conditions is legally superfluous, if the independent contractor relationship is not supposed to last for more than one month or if the above-mentioned information is contained in a written contract.

b. Day-to-Day Management of the Relationship

As mentioned above, the classification as an independent contractor relationship or a standard contract of employment does not only depend on the arrangements of the written contract or the statement of terms and conditions. Rather, the classification is subject to the manner in which the employee's services are effectively carried out on a day-to-day basis. Therefore, it is crucial that the employer remains cognizant of how the contractor is carrying out the indicia of their employment. In particular, the employer should be sensitive to whether the contractor's scope of employment is bleeding into the employer's basic organization structure. Recommended business practices dictate, at the very least, monthly written or oral evaluations or memoranda concerning the scope of the contracted party's employment to maintain records that may be used to refute a claim for re-characterization of employment.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Due to the obligations connected with Austrian employment law, employers in Austria tend to use different possibilities for drafting contracts. Therefore, Service Agreements and Work Service Agreements are frequently used. Moreover, the amount of temporary workers (*Leiharbeiter*) and fixed-term employment contracts (*befristete Arbeitsverträge*) is increasing. However, to avoid a circumvention of the Austrian employee protection legislation, the jurisdiction is strict in applying the abovementioned criteria for the classification as a standard Contract of Employment. Additionally, there are special rules in the Austrian Temporary Employment Act (*Arbeitnehmerüberlassungsgesetz*) to protect temporary workers from discrimination compared with regular employees.

Jurisdiction concerning Service Agreements, Work and Service Agreements and Employment Agreements.

As stated, the distinction between standard Contracts of Employment, Service Agreements and Work and Service Agreements depends on a case-by-case decision. The Austrian jurisdiction concerning the classification of doctors demonstrates this approach in an exemplary way.

Following the Austrian Jurisdiction, a doctor cannot generally be placed in one of the mentioned categories. Rather, the Jurisdiction distinguishes between the different arrangements of the respective contractual relationship. Therefore, a standard Employ-

ment Contract between a doctor and a hospital can only be assumed if the doctor is integrated in the organization of the hospital. The main factors here are based on the abovementioned criteria, regular working hours and official duties¹.

According to the Jurisdiction, the classification as a standard employee is therefore not justified in case of an attending doctor with flexible time management². The same is generally valid for a prison doctor. In this case, the Austrian Supreme Court stated that because of his professional duty, a doctor has to fulfill his responsibilities to the prison independently and under his sole responsibility. In particular, the classification as standard employee does not result from the restricted independence of the doctor, which is due to the security and the specific circumstances given in a prison³.

Furthermore, the contract between a doctor and his patient is generally qualified as Service Agreement⁴. However, if the doctor owes the patient only one specific task, the contract might be classified as Work and Service Agreement. Therefore, Austrian Jurisdiction assumes a Work and Service Agreement if the doctor's task only includes for example, the preparation and adjustment of prosthesis⁵.

Jurisdiction concerning Temporary Work

Temporary work means that the employees of a temporary works agency are lent out to work for another person. In this case, the temporary work agency continues to function as the employer. The person hiring the temporary worker generally does not have to fulfill all duties of an employer. However, in exceptional cases, it might be possible that an employment agreement is concluded between the hirer and the temporary worker as well.⁶ Whether this is the case or not, depends on a case-by-case decision based on the abovementioned criteria for the classification as an employment contract. However, to protect the employees from a circumvention of Austrian employee protection legislation, the jurisdiction is very strict in applying these criteria.

In case there is no Employment Agreement between the hirer and the temporary worker, the Austrian Temporary Employment Act must be kept in mind. That implies, amongst other things, obligations for the hirer such as compliance with safety regulations and the employer's duty of care.

Jurisdiction concerning Fixed-Term Employment Contracts

Another way employers try to reduce the risks associated with Austrian employee protection legislation is through the use of fixed-term employment contracts. The employment agreement ends with the expiry of the term agreed upon in this case.

Therefore, the employee loses the protection against dismissal granted by Austrian legislation. To avoid a circumvention of these regulations, there are certain limits to fixed-term employments. On the one hand, there are limitations concerning particularly long periods of fixed terms. On the other hand, the employer is obliged to protect employees under a fixed-term contract against discriminations compared with permanent employees. Finally, the fixed-term agreement has to be objectively justified. In particular, as mentioned above, it is impermissible to string together a large number of fixed-term employment contracts without an objective justification. In this case, the agreement on a

fixed-term employment is void. Therefore, the employee may have a claim for a re-characterization of the contract. Again Austrian jurisdiction is very strict when it comes to the

¹ Judgment of the Austrian Supreme Court of 13 July 1976 (case reference 4 Ob 27/76).

² Judgment of the Austrian Supreme Court of 29 September 1981 (case reference 4 Ob 45/81).

³ Judgment of the Austrian Supreme Court of 10 July 2008 (case reference 8 ObA 55/07g).

⁴ Judgment of the Austrian Supreme Court of 4 July 1991 (case reference 6 Ob 558/91).

⁵ Judgment of the Austrian Supreme Court of 12 March 1991 (case reference 5 Ob 514/91).

⁶ Judgment of the Austrian Supreme Court of 7 February 2008 (case reference 9 ObA 2/08x).

question of an objective justification. Therefore, special social or economic reasons are required to justify consecutive fixed-term contracts.

b. Recent Amendments to the Law

In 2016 the Anti-Social-Fraud Act (*Sozialbetrugsbekämpfungsgesetz*) came into force and serves to prevent and pursue social fraud, in particular activeness by bogus firms. With these legal regulations many actions are criminal offence, like

- withholding of contributions to the insurance institutions,
- registration at the social insurance agencies with fraudulent intent (e.g. registration knowing that the contributions will never be paid),
- organized illegal employment and undeclared work.

If there is a concrete suspicion of illegal actions, the Austrian authorities can request further information at the database for social fraud (*Sozialbetrugsdatenbank*), an institution at the Ministry of Finance. The main focus lies on entities within the construction industry. Therefore, a new competence center for social fraud (Kompetenzzentrum LSDB) was created. In addition to the above-mentioned activities, the catalogue of social fraud has been extended by misuse of sick leave, benefit abuse and unlawful use of the e-card (electronic administration system).

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

In case of cross-border action foreign enterprises may be subject to Austrian taxation. Generally, an enterprise, which engages standard employees within the Austrian borders, has to redirect income taxes as required by Austrian tax law. On the contrary, the enterprise does not have to pay taxes if it engages independent contractors such as brokers, general commission agents or other agents of an independent status. This complies with the fact that independent contractors are generally obliged to settle their income tax payments by themselves. Therefore, in this case, the foreign enterprise itself is not affected by Austrian tax law. However, there may be exceptions or specific regulations in the double taxation agreement between Austria and the respective country. Therefore, a foreign enterprise should seek legal advice concerning the question of whether there is a double taxation agreement and whether this contains any exceptions or special regulations relevant for the individual case.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

As mentioned in the preceding chapter, an enterprise, which engages standard employees within the Austrian borders, has to redirect income taxes as required by Austrian tax law. This applies regardless of whether or not the particular enterprise has a permanent establishment in Austria. However, as stated above, there may be special regulations in the double taxation agreement between Austria and the respective country. Additionally, the foreign enterprise is generally obliged to contribute to the social insurance of a standard employee. Since the precise conditions depend on a case-by-case basis, it is advisable in any case, to seek legal advice when engaging standard employees within the Austrian borders.

VII. CONCLUSION

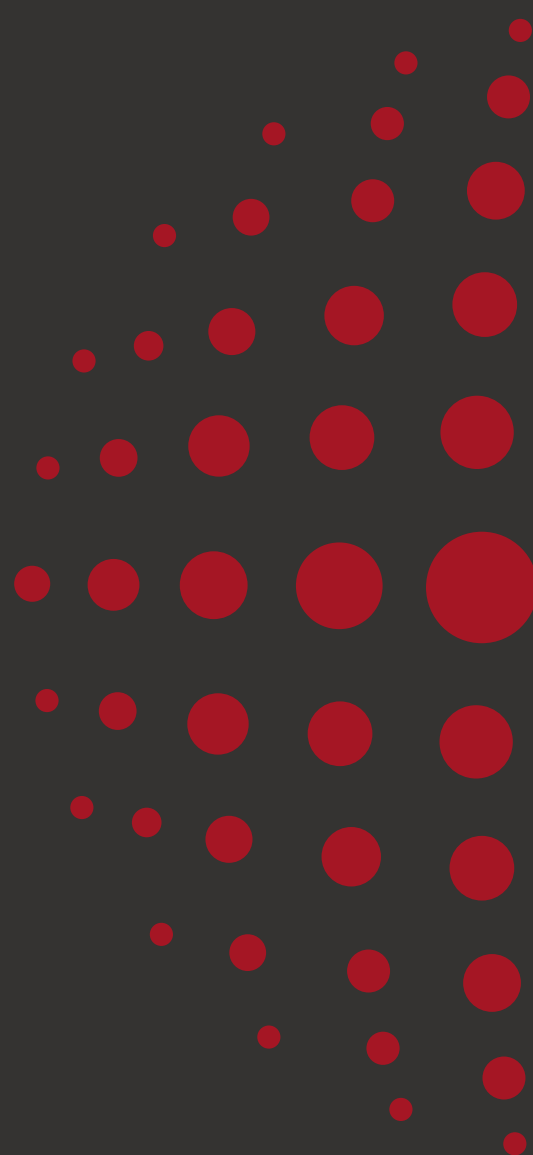
As stated above, an independent contractor employment relationship does not require a written contract. However, to clearly define an employment relationship from the outset, an employer should issue the contractor a written statement of terms and conditions (*Dienstzettel*). This statement of terms must include basic information regarding the employment arrangement, including the names of the two parties, basic salary or wages, date that the arrangement commences, and any classification within the labor system. This written statement of terms is often required for the employee to register for social insurance, if they are seeking to do so independent from their employer.

In addition to this contract, an employer should remain cognizant of how the contractor is carrying out the indicia of their employment and remains sensitive to whether the contractor's scope of employment is bleeding into the employer's basic organization structure. Recommended business practices dictate, at the very least, monthly written or oral evaluations or memoranda concerning the scope of the contracted party's employment to maintain records that may be used to refute a claim for re-characterization of employment.

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BELGIUM

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I. OVERVIEW

a. Introduction

A worker who has an employment contract is considered to be an employee. There are three essential elements making up an employment contract: work, remuneration and relationship of authority. The third element is the critical characteristic.

Independent contractors are referred to as “self-employed workers” in Belgium. A self-employed worker is any individual performing professional activities within the scope of which he/she does not work under the authority of an employer. Consequently, the criteria for distinguishing between a self-employed person and an employee are based on the existence or the absence of a link of subordination between the contracting parties: if one of these parties exercises an employer’s authority over the other, the employment relationship is deemed to be an employment contract.

Before 1 January 2007, the guidelines for distinguishing employees from independent contractors were based on the jurisprudence of the Court of Cassation (Belgian Supreme Court), which rendered several important decisions in this matter. The Belgian government nevertheless decided to regulate this matter at the end of 2006, with the so-called “Employment Relations Act of 2006”¹, which was primarily a reflection of the jurisprudence of the Court of Cassation.

Since mid-2013, the parties to an employment contract, or the self-employed person who seek(s) legal certainty with respect to the working relationship, can request a social ruling from the Administrative Commission on Employment Relations (“Social Ruling Commission”) in order to reduce the risk of re-characterization and to avoid the related sanctions.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The Employment Relations Act created a legal framework to ascertain the legal nature of the employment relationship. The key test remains whether or not there is a relationship of authority/subordination between the parties. The new element introduced by the Act is that the intention of the parties (and therefore the mutually agreed legal status) constitutes the essential factor to determine whether or not a subordinate relationship exists. This is in line with the established case law of the Court of Cassation. Under this Act, re-qualification of the relationship (from self-employed to employee) and the resulting obligation to register with a different social security status, will only be possible in cases where certain factual elements are found to be incompatible with the qualification chosen by the parties.

The Act defines the four **general criteria** to be used in determining whether such factual elements exist in a particular case:

- *the parties’ intention as expressed in the agreement*: the qualification decided by the parties will be the starting point for the judge’s analysis of the nature of the contract; however, it is understood that the actual performance of the agreement must be in line with the nature of the employment relationship chosen by the parties.
- *the worker’s freedom to organize his/her own working time*: impossibility of freely organizing working time; obligation to strictly follow working days (performing

¹ Title XIII of the Program Act of 27 December 2006, OG 28 December 2006.

- a given number of hours, reporting any absence); execution of specific orders regarding specific tasks – all of these are elements that point to subordination.
- *the worker's freedom to organize his/her work*: in the framework of self-employment, parties enjoy a wider degree of freedom regarding the organization and the practical execution of the work, even if it is accepted that general guidelines may be given to accommodate the requirements of the job itself (e.g. the opening and closing hours of a shop which, although placing an obligation on an independent contractor, do not necessarily indicate subordination). The absence of any obligation to justify the time schedule, freedom to work the number of hours of choice, complete freedom to choose the dates of annual vacations – all of these elements, in principle, indicate self-employment.
- *the ability to exercise hierarchical control*.

The Act also provides **neutral criteria** that are not relevant for determining the nature of the employment relationship. These criteria relate to a number of legal elements, which are mere formalities and concern the manner in which the contracting parties organize their relations with the social and tax administration. They contain no information regarding the way in which the parties perform the employment relationship. These criteria include the title of the contract, registration with a social security office, and registration with the Cross point bank for Enterprises, registration with the VAT administration, and the way in which the revenue is reported to the tax authorities.

Besides the general criteria, the Act also determined a list of **specific socio-economic criteria**, which apply in addition to the criteria listed above. They may not deviate from either the general or the neutral criteria laid down in the law. The Act sets out a number of examples: the possibility of hiring or replacing employees, working in places or with materials which are personal property, guaranteed pay, personal and substantial investment in the enterprise with personal capital, power of decision over financial resources. The Act also provides a procedure for establishing these or other specific criteria in a determined sector or profession, or categories of professions by Royal Decree.

By means of an Act, in 2012, the Government reinforced its effort to counter bogus self-employment in some fraud-sensitive sectors, by introducing a refutable presumption (which can be reversed by all means of law) of the existence of an employment agreement, if, based on the contractual relationship, more than half of the following criteria are fulfilled:

- i. Absence of any financial or economic risk for the worker, such as absence of a personal and substantial investment with his/her own resources in the undertaking, or absence of a personal and substantial part in the profits or losses of the undertaking;
- ii. absence of liability and decision-making power in respect of the financial resources of the undertaking;
- iii. absence of power of decision in respect of the purchase policy of the undertaking;
- iv. absence of power of decision in respect of the price policy, unless prices are fixed by law;
- v. absence of commitment in respect of the result of the agreed work;
- vi. guaranteed payment of a fixed compensation without regard to the result of the undertaking or the volume of the work performed;
- vii. not being an employer of personally and freely hired staff, or absence of possibility to hire personnel to carry out the agreed work or to be replaced;

viii. not acting as an undertaking towards other individuals or working usually or mainly for the same contractual partner;

ix. working in spaces of which one is not the owner or tenant, or working with materials provided, financed or secured by the contractual partner.

These criteria can be modified for per (sub)sector by Royal Decree.

Currently, the presumption only applies to:

- the construction industry;
- security and monitoring/surveillance activities on behalf of third parties;
- transport of goods and/or passenger transport on behalf of third parties, with exception for ambulance services and transport for disabled persons;
- activities falling within the scope of the Joint Committee for the cleaning sector.

b. General Differences in Tax Treatment

Income tax

For the contractor of the self-employed worker, payment of the agreed remuneration will be made directly to the worker, without any required tax withholdings (however, in most cases, the value added tax will be generated). This means that the independent contractor is personally responsible for the tax obligations. Within the framework of an employment contract, mandatory source deductions must be made by the employer.

The level of income taxation for employees and self-employed individuals is similar. The income tax rate is progressive (the more the worker earns, the higher the tax rate). However, an independent contractor can benefit from some tax advantages, for example, in the field of the writing of business expenses or by working through his own management company.

Social security contributions

The employer is responsible for the registration, declaration and payment of both the employee and employer's social security contributions. The employee does not have to pay his social contributions by himself. The employer retains, each month, 13.07 % of the gross salary as personal social security contributions and pays a maximum of 35 % of the gross salary as employer's contributions. In total, the social security contributions represent around 48 % of the gross salary of an employee (this stands for white-collars only, employer's contributions on blue-collars are higher).

The self-employed person must register himself to a social insurance fund by the time he begins his activities. He will pay his own social contributions of approximately 21 %, every three months, to his social insurance fund. Contrary to employees, the social security contributions of a self-employed person are capped (i.e. beyond a certain amount of income).

c. Differences in Benefit Entitlement

Employment benefits

Legally, independent contractors are not entitled to specific benefits. They normally only receive the remuneration agreed between the parties.

Apart from the base fixed salary, an employee will be entitled to benefits provided by law, such as, for example: Holiday leave and pay; End of year premium; Public holidays; overtime pay.

Social security benefits

The employer's and employee's social security contributions are used to pay:

- allowances in the event of sickness;
- unemployment benefits;
- allowances in the event of incapacity for work through sickness or invalidity;
- allowances in the event of accidents at work;
- allowances in the event of industrial disease;
- family allowances;
- retirement and survival pensions.

The self-employed worker's contributions are fixed at a lower percentage than the joint contribution of employers and employees, and provide fewer rights. The independent contractor's benefit entitlement covers four social security branches:

- *family benefits*, which includes childbirth or adoption allowance, monthly family benefits, and others benefits such as age-based supplementary payments and orphan allowance;
- *retirement and survival benefits*;
- *sickness and incapacity insurance*: covering some healthcare needs and incapacity for work (the self-employed person is required to register with the insurance fund of his choice);
- *social insurance in case of bankruptcy*: this insurance will allow the self-employed person to maintain his rights regarding healthcare insurance and family benefits for four quarters, and allow him to obtain temporary compensation.

In addition, the self-employed person will also benefit from a maternity insurance. As a rule, a self-employed person is not entitled to receive unemployment benefits, contrary to employees. It should be noted that the legislation on social security for independent contractors also applies to their caregivers. The caregiver is a person who, in Belgium, assists or supplies an independent contractor during the exercise of his function, but who is not engaged to him with any type of contract. The spouse of the independent contractor, or the person having made a declaration of legal cohabitation (provided that they do not have a professional activity as employee or independent) will automatically be considered as a caregiver and therefore, benefit from all the rules. This presumption is rebuttable.

d. Differences in Protection from Termination

The general termination modes of contractual relationships are the same for employees and self-employed persons. This stands, for example, for termination by mutual agreement, force majeure or judicial resolution of the contract.

However, for employees, there are a set of legal rules restricting the possibility to unilaterally terminate their employment contract. Apart from the dismissal for serious cause, there are two methods of termination of an employment contract concluded for an indefinite period of time: either by giving notice or by paying severance compensation in lieu of notice. The duration of the notice period is, in principle, fixed by law and depends mainly on the seniority of the employee concerned.

It is important to note, that some employees benefit from a specific protection against dismissal based on their individual situation (e.g. maternity, trade union activities, complaint against sexual or moral harassment, etc.). Depending on the case, the protection involves procedure or motivation requirements and is sanctioned by a specific termination indemnity fixed by law.

As a rule, there is no requirement to ask a court for permission to dismiss, except in very exceptional circumstances (e.g. for employees involved in trade union activities and representing the personnel in the Works Council, the Committee for Prevention and Protection at Work and/or the Trade Union delegation). Even under these exceptional circumstances in which prior approval would be required, not asking for approval will never result in the nullity of the dismissal itself. The sanctions that are imposed are only of a pecuniary nature.

With regard to the termination, it is clear that there is a higher degree of flexibility when working with a self-employed person, in comparison with the protective and mandatory legal rules applicable to employees. As a rule, a self-employed person does not benefit from any legal protection from termination, unless otherwise agreed between contracting parties. In absence of such protection rules, parties will have to take case law into consideration when determining the termination rights (notice period, compensation).

e. Local Limitations on Use of Independent Contractors

There are no specific local limitations on the use of independent contractors. However, the independent contractor will be assumed to work as an employee within the framework of the Act of 3 July 1978 relating to employment contracts, which provides that *"Benefits of additional services performed under a contract of services are presumed to be done under an employment contract, without that the evidence of the contrary can be made, and this when the service provider and the recipient of these are bound by an employment contract for the performance of similar activities"* (free translation). In other words, a worker can, in principle, not work as an employee and as a self-employed person for the same company.

f. Other Ramifications of Classification

Employees who have been struck by the closing-down of their company can benefit from the intervention of the "Indemnity Fund for the Closing-down of Firms" (IFCF).

The IFCF is mainly financed by employer's contributions and reimbursements by receivers and liquidators of the amounts that were advanced to the employees. In addition, the IFCF receives limited funding from the Belgian government.

In practice, the IFCF pays the amounts payable to the employees and recovers them afterwards from the receiver(s) and liquidators.

The IFCF intervenes in case of bankruptcy, take-over after bankruptcy, conventional transfer, liquidation and closing-down. Following certain legal criteria, it pays different kinds of indemnities to the employees: closing-down indemnities, contractual indemnities, transition indemnities, company bonuses and additional remunerations due to certain protected employees.

g. Leased or Seconded Employees

Under Belgian law, the lease out of employees is governed by the Act on temporary work. This Act prohibits, in principle, activity that consists of a natural or legal person leasing his employees to third parties who use these employees and exercise over them, any part whatsoever, the authority belonging to the employer. The violation of this prohibition can lead to civil, criminal and administrative sanctions.

This Act provides, however, for some exceptions. In certain cases, an exceptional leasing of employees is indeed permitted, subject to the respect of general conditions and the warning to, or prior authorisation of, the Labour Inspectorate. Those general conditions are:

- *Exceptional character*: the leasing of employees must be of an exceptional character, which means that it must be both limited in time and not be repetitive.
- *Permanent employees*: the leased employees must be permanent employees, i.e. persons who are already in the employ of the employer who leases them and who work regularly for him.
- *Level of remuneration*: the remuneration and fringe benefits of the leased employees cannot be inferior to those from which employees carrying out the same functions within the user company benefit.

If the above-mentioned general conditions are fulfilled, it is possible to obtain authorization by the Labour Inspectorate. To this end, a specific procedure must be followed and a written document must be signed by the employer, the user and the worker, before the start of the leasing.

It is also possible to have recourse to the leasing of employees by means of simple prior information to the Labour Inspectorate in two hypotheses:

- within the framework of collaboration between companies of the same economic or financial entity (groups, holding);
- for the execution, on a temporary basis, of specialised tasks requiring a specific professional qualification.

In these hypotheses, the signature of a written document by all parties prior to the leasing is also required.

The legal leasing of employees not only implies that the contract between the employee and his/her employer continues to be legally valid and in force, but also that the user becomes jointly liable with the employer for the payment of social security contributions, remuneration, indemnities and benefits, which derive from the employment contract.

In case of illegal leasing, both the employer and the user are potentially exposed to civil, administrative and/or criminal sanctions.

The civil sanctions laid down by the Act on temporary work are the following:

- the employment contract between the employee concerned and the employer (i.e. the entity which leases the employee) is void as of the moment the employee starts working for the "user";
- the user and this employee are bound, as of that moment, by an open-ended employment contract;
- the employee can terminate this contract without notice, nor indemnity, until the date on which he/she would normally no longer be at the disposal of the "user"; and
- the user and the employer (i.e. the entity which leases the employee) are jointly liable for the payment of social security contributions, remuneration and benefits deriving from this open-ended employment contract.

The administrative or criminal sanctions laid down by the Social criminal code, include a criminal fine of EUR 600 to EUR 6,000 or an administrative fine of EUR 300 to EUR 3,000. These amounts apply per employee, but are limited to a maximum of respectively EUR 600,000 or EUR 300,000 in total.

Besides, the Supreme Court ruled, in a judgment of 15 February 2016, that an employer who leases out his employees to a user in violation of the prohibition to lease out employees, in principle, imposed by the Act on temporary work, might be unable to rely on the contract, which formalizes such a leasing out, in order to claim the payment of

his bill by the user.

An alternative to the leasing of employees could be to have recourse to a service agreement between the companies concerned.

In such a framework, a user company gives limited instructions to employees of a service provider working within the user company, based on a service agreement executed between the user company and the employer/service provider. The purpose of the said agreement is not the lease out of employees, but the execution of a determined work.

However, the following conditions must be simultaneously met:

- the service agreement must be in writing and clearly, and in detail, list the exact types of instructions that can be given to the service provider's employees by the user company (the types of instructions will depend on the work to be performed and on the functions concerned and must cover all aspects thereof, which could result in an extensive service agreement; e.g. attendance to meetings; preparation of documents on a determined topic; respect of deadlines; etc.);
- these instructions may not undermine the legal employer's authority over the employees;
- the factual situation must correspond to the wording of the service agreement.
- If any of these conditions are not met, there will be a prohibited lease of personnel.

h. Regulations of the Different Categories of Contracts

Belgian labour law is very protective and many aspects of the employer/employee relationship are regulated by federal legislation and collective bargaining agreements. With regard to employment contracts as such, the main rules are stipulated in the Act of 3 July 1978 relating to employment contracts, which contains the major provisions in that matter. This Act regulates the conclusion, the execution and the termination of the contract, be it a contract for an indefinite or a definite period. It also regulates specific situations such as, for example, the salesman agreement, the domestic agreement and the homework agreement. Moreover, this Act contains provisions about the duration and the suspension of the contract, the obligation of both parties, the termination of the contract, the non-competition clause, etc. Another important legal source is the Act on Work, which mainly deals with working time issues. What is not specifically regulated by labour law is subject to general civil law.

Agreements concluded with self-employed persons are generally much less regulated. There is no specific global Act about the self-employment relationship. The general civil, commercial and corporate laws will apply. However, certain types of contracts concluded with a self-employed person are legally regulated (e.g. the Commercial agency agreement), but it is rather uncommon.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Such a re-characterization can only be established by a Court. Re-characterization of the relationship (from self-employed to employee) and the resulting obligation to register with a different tax and social security system, will only be possible in cases where certain factual elements are found to be incompatible with the qualification chosen by parties. Indeed, since 2003, and following several decisions of the Court of Cassation, the judge will have to first determine how the parties have qualified their relationship,

so that the will of the parties and the qualification of the contract are the pre-eminent criteria, and this qualification can only be re-characterized if there are elements incompatible with the chosen qualification.

b. The Legal Consequences of a Re-Characterisation

Principle - in case of a re-characterization, there are several legal consequences; both for the self-employed person and the other party as regards to tax, social security, and labour relations.

Tax law - the Company (i.e. the employer) could be held liable for not having withheld personal income taxes. Tax increases and fines can be imposed. However, contrary to the social security contributions, the company will not become solely liable for the taxes. If the authorities demand the payment of the taxes from the company, the latter will have recourse against the employee for the amounts paid (provided the employee is still solvent).

The Tax Office could claim such amounts for a period of 3 years (or 5 years in case of fraud) preceding the re-characterization. The amounts due before this date are barred. It must be noted that the Office could claim a tax on secret commissions, equal to 103 % of the amounts that were not mentioned on the fiscal statement – which was naturally not delivered by the employer.

Social security – Basic approach – the corresponding social security scheme will be applied, taking into account the applicable prescription period. This means that, as a rule:

- the Company could be held fully liable for the entire amount of social security contributions that should have been paid, i.e. 13,07 % employee contributions and approximately 35 % employer contributions of the fees paid, to be increased with interest (7%), penalties and an increase of 10 %. There is no possibility of recovering the amounts so paid from the employee concerned (any contractual stipulation to the contrary would be null and void).
- moreover, criminal sanctions (fines) could also be imposed for not declaring the employment to the National Office for Social Security (NOSS).
- The NOSS could claim such amounts for a period of 3 years (or 7 years in case of fraud).
- Social security – Derogations – however, since January 1st 2013, the re-characterization has fewer consequences for the employer in the field of social security and this in two cases:
- when the employee voluntarily registers with the NOSS (in a specific notice);
- when the parties obtained a social ruling from the Administrative Commission on Employment Relations (see “t” below).

In these two cases (only), some reductions are possible with regard to the claimed amounts, the regularization in time and the calculation basis. Criminal sanctions are also excluded.

Labour law – the whole relationship will be qualified as an employment contract from the beginning. As a consequence, the worker will have the right to claim arrears of certain benefits, such as holiday pay, end of year premium, salary increases provided by law, salary for overtime work, etc. The worker could also claim a legal severance indemnity in case of termination.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

Most of the time, it is when the independent relationship comes to an end and the individual concerned starts legal proceedings, that a Labour Court will examine the qualification given by the parties to the contract as well as the concrete terms of the relationship. When there are sufficient elements that are not compatible with the chosen qualification of the contract, it will be re-characterized as an employment contract and the individual concerned will be granted several amounts specific to the execution and the termination of the employment contract (e.g. arrears of salary, termination indemnities).

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In addition to the tax, social security and labour law consequences as described above, the employer is, in case of re-characterization, exposed to financial sanctions provided by the Criminal Social Code, for example, due to the lack of:

- declaration to the National Office for Social Security;
- payroll documents;
- work accident insurance;
- work Rules;
- holiday pay.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

It is recommended to draft a written agreement. This agreement should take into consideration the general criteria provided by the Act, as described above. In other words, it should be clearly stipulated, for example, that the worker is free to organize his/her work and his/her working time. The relationship should be structured in such a way as to include as many independent factors as possible, while avoiding elements specific to a subordinate relationship. The written agreement will play a significant role in establishing the nature of the relationship. In addition, it is recommended to include specific clauses such as termination provisions.

b. Day-to-Day Management of the Relationship

The management of the day-to-day relationship must be consistent with its contractual qualification. Therefore, exercising close control on the work performed and giving detailed instructions must be avoided. Only general directives should be transmitted from the principal to the individual. The principal should give the worker as much independence as possible.

For example, in a decision of 6 December 2010, the Court of Cassation ruled that monitoring the quality of work is allowed. However, such control cannot go beyond a standard control of the quality of the delivered work and must stay in line with the independent qualification of the relationship. This implies that only the result can be controlled.

In its decision of 10 October 2016, the Court of Cassation ruled that the ability of one party to discipline or sanction the other party, renders the independent nature of the cooperation between those parties impossible.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Several Belgian authors have already mentioned that some of the nine specific criteria introduced by the Act of August 25, 2012, could be difficult to apply in practice. For example, the criteria *“Not acting as an undertaking towards other individuals or working, generally and habitually, for one contracting party”* could be interpreted as an alternative criterion, but also as a cumulative criterion. In addition, several criteria refer to the notion of “undertaking”, but if the self-employed person works through an intermediary undertaking (i.e. his/her own management company), it is not clear whether the criteria refer to the self-employed person’s undertaking, or to the main undertaking (i.e. the principal).

Consequently, the National Labour Council (Nationale Arbeidsraad – Conseil National de Travail) has been asked by the federal government to evaluate both the general and sector-specific criteria, as these criteria are often found to be difficult to apply in some circumstances. For example, in certain cases the specific criteria may point in the direction of self-employment, whereas the general criteria may indicate the opposite. Also, the current set of criteria do not seem to be adapted to more contemporary forms of (self-)employment, such as services performed in the sharing economy. A report of the National Labour Council is expected in the beginning of 2017.

b. Recent Amendments to the Law

As previously mentioned in the Introduction, since mid-2013, the parties to an employment contract, or the self-employed person who seek(s) legal certainty with respect to the working relationship, can request a social ruling from the Administrative Commission on Employment Relations (“Social Ruling Commission”) in order to reduce the risk of re-characterization and to avoid the related sanctions.

This ability can be used prior to beginning the relationship or during the first year. The ruling is valid for a period of three years. The final decision-making power to re-characterize an independent relationship into an employment agreement rests with the Labour Courts. However, the consequences of such re-characterization will be less severe, at least concerning social security matters, if the employer has obtained a social ruling.

Until 1 January 2016, the Social Ruling Commission rendered 48 decisions; a limited amount, which has decreased over time. Although useful in circumstances where there is a lot of legal uncertainty, the possibility to apply for a social ruling seems to have little success.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

With regard to permanent establishment, Belgian regulations are generally consistent with those of the Organization for Economic Co-operation and Development (“OECD”) in its Model Tax Convention. The Belgian authorities issued a *“Standard agreement for the avoidance of double taxation with respect to taxes on income and on capital and for the prevention of fiscal evasion”*, based on the OECD Model. This matter is also regulated by the Belgian Income Tax Code 1992.

According to the said Code, “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried on. Specifically, this includes: a place of management; a branch; an office; a factory; a workshop; a mine, an oil or gas well; a quarry or any other place of extraction of natural resources. A foreign company would be deemed to have a Belgian establishment if, for the same or related projects, it carries out services in Belgium through one or more individuals (that are present in Belgium) for, in total, more than 30 days during any 12-month period.

However, “permanent establishment” shall be deemed not to include:

- the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
- the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery, or of processing by another enterprise;
- the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or collecting information for the enterprise;
- the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character;
- the maintenance of a fixed place of business solely for any combination of certain activities, provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

An enterprise shall not be deemed to have a permanent establishment merely because it carries on business through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

Under Belgian Double Tax Convention law, a dependent agent will only give rise to a permanent establishment if he has, and habitually exercises, authority to conclude contracts on behalf of its foreign principal. Independent agents acting in the ordinary course of their business do not give rise to a Belgian establishment.

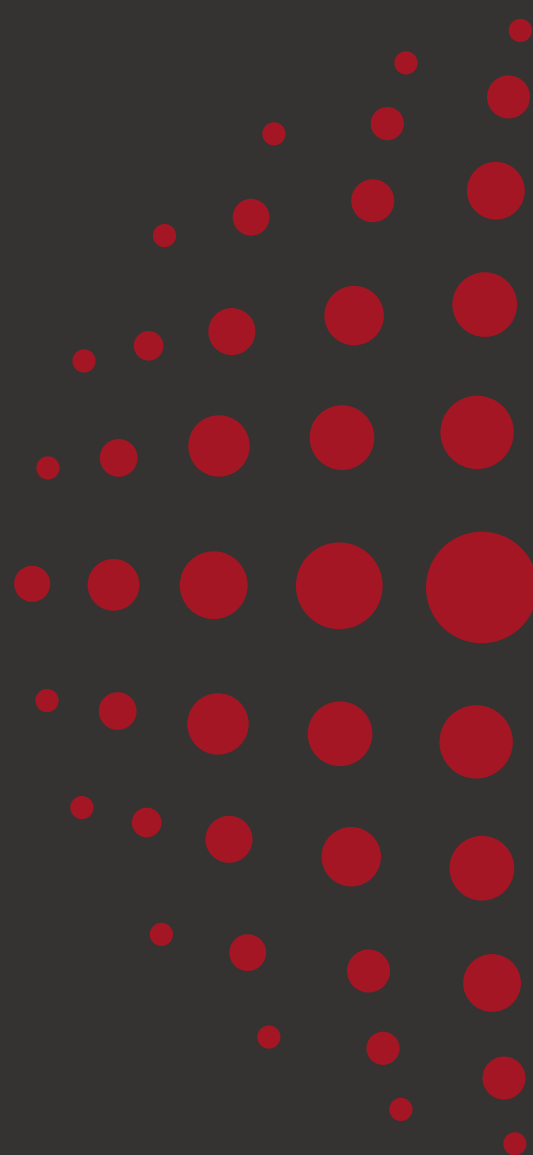
b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

The same principles under point a. above will apply. The employment of one or more individuals may create a permanent establishment where there is either a fixed place of business, or where business is conducted via a dependent agent. The ramifications include that the foreign company will have to pay taxes in Belgium on its business profits attributable to the permanent establishment.

VII. CONCLUSION

Since the Act of December 27, 2006, a legal framework exists in Belgium to ascertain the legal nature of the employment relationship, and details specific criteria used to determine and subsequently qualify the contractual relationship: general criteria, neutral criteria (that are not relevant for determining the nature of the relationship), as well as criteria that particularly applies to certain sectors of industry.

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BRAZIL

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I. OVERVIEW

a. Introduction

In Brazil, labor relations are a matter of Federal law, which gives Brazil's individual States and Municipalities no power to legislate over labor matters. Despite the huge dimension of the country, labor rights are nationally standardized. The same labor costs and principles will apply regardless of an employer's place of business.

The basic principles of Brazil's labor relations laws are set out in the Federal Constitution, Labor Code, the commonly referred to "CLT" (Consolidação das Leis do Trabalho) and a number of specific federal laws and regulations. Labor rights established by such laws are mandatory and cannot be negotiated between the parties if the end result of the negotiation is detrimental to the employees.

In addition to legislation, some basic principles implicitly or expressly provided by law will govern any employment relationship in Brazil. Among them, the principle of "Prevalence of Facts" is the most relevant in the analysis of an Employee versus Independent Contractor relationship. This principle provides that in the determination of labor issues, the relevant facts surrounding a relationship will prevail over any formal documents executed by the parties.

In Brazil, workers may be hired in several ways but the most common practice is the hiring of workers as employees. However, the parties may also structure the relationship in other ways, such as independent contractors/consultants, outsourced workers, temporary workers, interns and non-employed officers, among others, provided that the specific rules and regulations regarding such alternatives are complied with.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

An employee is defined by the Brazilian Labor Code (CLT) as an individual who renders services to an employer on a permanent basis, under its direction and for a salary. Professional subordination of the employee to the employer is essential in an employment relationship.

On the other hand, an independent contractor relationship is regulated by the Brazilian Civil Law, which establishes that any company may enter into a contract with an individual to render services as an independent contractor. A consultant hired as an independent contractor would and should be free to determine how and when the work is performed. An independent contractor does not usually perform work that is necessary for the company on a permanent basis.

Brazilian Labor courts have determined that factors, which indicate subordination include the lack of self-determination to decide how the work should be done; the control of hours of work; and the obligation to present reports and to observe previous targets.

b. General Differences in Tax Treatment

Independent contractors may act either as an individual or as a legal entity duly incorporated by the individual, leading to different taxation and obligations. By law an employee must be an individual. Depending on the alternative, the social security and taxation differ as follows:

	EMPLOYEE	INDEPENDENT CONTRACTOR	
		INDIVIDUAL	LEGAL ENTITY/COMPANY
Social Security Contribution due by the contracting party	Employers must pay to the Government social security contributions at approximately 28% on the total monthly compensation paid to their employees, without a cap.	The contracting party must pay social security contributions to the Government at 20% on the total monthly compensation paid to the independent contractor, without a cap.	There is no social security contribution on the fees paid to a legal entity.
Social Security Contribution due by the professional	Social security contributions due by employees are equivalent to 11% of their monthly remuneration, limited to approximately BRL 600.00*. This amount should be deducted by the employer from the employees' remuneration and paid to the Government.	Social security contributions due by independent contractors are equivalent to 11% of their monthly remuneration, limited to approximately BRL 600.00*. This amount should be deducted by the contracting party from the remuneration and paid to the Government.	As a partner of a legal entity, the individual should pay his/her own social security contribution.
Individual income tax	Employers must withhold income tax from the employees' monthly remuneration and pay it to the Government, according to a progressive rate, which can reach up to 27.5%.	The contracting party must withhold the income tax from the independent contractor's monthly compensation and pay it to the Government, according to a progressive rate, which can reach up to 27.5%.	There is no individual income tax. There are different corporate taxes to be borne by the legal entity.

(*) the cap is adjusted every year

c. Differences in Benefit Entitlement

Independent Contractor

In a relationship with an independent contractor, the parties are free to negotiate the terms and conditions, including possible benefits and any other conditions. There is no minimum remuneration or conditions, which must be observed by the parties.

Employees

In an employment relationship, the employer must observe the minimum conditions established by law and by the applicable collective bargaining agreement. Employers and employees are all mandatorily represented by a specific union in Brazil. Among the obligatory labor rights and obligations it is worth highlighting:

i. FGTS – Severance Pay Fund: all employers in Brazil must deposit an amount equivalent to 8% of the employees' monthly compensation into a special account opened with the Federal Savings Bank on behalf of each of the employees. This special account is the FGTS (severance pay fund).

In the event of termination without cause, retirement, or serious illness, among other situations, the employee is entitled to withdraw the balance of the FGTS account including any additional termination indemnification, as the case may be.

ii. Annual Paid Vacation: after each 12-month working period, an employee is entitled to 30 days' paid annual leave, which must be taken within the subsequent period of 12 months. In addition to the ordinary pay over the period of annual leave, the employee is entitled to receive a vacation bonus equivalent to one-third of his/her [annual] compensation.

iii. 13th month Salary or Christmas Bonus: besides the annual salary paid over 12 months, employees in Brazil are entitled to a 13th month salary (Christmas bonus) at the end of the year.

iv. Transportation voucher: employees who use the public transport system to commute between home and the workplace are entitled to transportation vouchers.

v. Working hours: any regular working period may not exceed eight hours per day and 44 hours per week. Overtime is permitted provided employees are duly remunerated with an additional amount equivalent to at least 50% of their normal work-hour rate and provided the total work hours do not exceed 10 hours per day. Employees in a position of trust (such as management) are not entitled to overtime, nor are they subject to controlled working time. Certain special categories have a shorter limit of daily working hours.

vi. Other benefits: Although they are not compulsory by law, it is common market practice in Brazil to grant meal vouchers and health care. It is also common practice to provide private pension plans, life insurance and education allowances. Collective bargaining agreements may provide for additional compulsory benefits.

Employee benefits and conditions are vested rights, and employers are prevented from changing employment terms and conditions to the employee's detriment, whether or not the employee has previously consented to such change.

d. Differences in Protection from Termination

Independent Contractor

In a relationship with an independent contractor, the parties are free to negotiate the terms and conditions, including a termination process (types of termination, with or without cause, prior notice, post-termination conditions, etc.). According to the Civil Code, an independent contractor agreement can be terminated by any party, by giving the other party prior notice of a minimum of:

- eight days if the remuneration is paid on a monthly basis;
- four days if the remuneration is paid on a weekly or fortnight basis; and
- one day if the contract is valid for less than seven days.

Any other conditions should be negotiated by the parties. It is common practice for the parties to negotiate a minimum 30 day notice period. Employees

Employees

Employment contracts in Brazil are usually for an indefinite term. An employer may terminate an employment agreement at any time, with or without cause, and an employee can also resign at any time.

The party terminating the employment contract must give notice to the other party, both in the case of resignation or termination without cause. Minimum notice to be given by the employer depends on length of service: 30 days' notice for employees with up to one year of service at the same company, plus three days for each additional year of service, subject to a maximum of 90 days. Prior notice to be given by employees to their employer has been limited to 30 days by the courts.

Termination for cause must be based on misconduct established by law and does not require prior notice.

Employees whose circumstances put them in a position of "temporary job instability" cannot be dismissed without cause, e.g. union representatives, the members of the Internal Committee for Accident Prevention (CIPA), expectant mothers and employees injured due to workplace accidents, among other specific situations.

The table below sets out the various mandatory severance payments due to an employee. Entitlement to these payments varies depending on the mode of termination, whether by resignation / termination with or without cause.

MANDATORY SEVERANCE	COMMENTS	TYPE OF TERMINATION		
		RESIGNATION	WITHOUT CAUSE	WITH CAUSE
Prior notice	Proportional to the length of service, minimum of 30 days and maximum 90 days. Employee prior notice is limited to 30 days by courts. Prior notice period may be worked or paid in lieu of notice.	√	√	X
Christmas Bonus	1/12 of monthly compensation per month of work during the calendar year, including the prior notice period	√	√	X
Vested and Proportional Vacation not taken	All employees are entitled to 30 days paid annual leave after 12 months of work. During the vacation period an employee is entitled to his/her regular salary plus 1/3 vacation bonus.	√	√	Only vested vacation; not the proportional vacation
FGTS Withdrawal and FGTS Indemnification	FGTS (Severance Pay Fund) is a fund constituted of amounts equivalent to 8% of employees' monthly compensation and deposited monthly by the employers into a special account opened with the Federal Savings Bank on behalf of the employees. Employees may withdraw the FGTS balance in situations, such as termination without cause, retirement, serious illness, among others. FGTS Indemnification corresponds to an amount equivalent to 50% of the FGTS account's balance: 40% is due to the employee and 10% is due to the Government.	√	X	√
Indemnification equivalent to one monthly salary	If a termination without cause occurs 30 days before the annual salary review negotiations	√	X	√

In addition to the above, collective bargaining agreements may establish additional termination rights.

e. Local Limitations on Use of Independent Contractors

Any company may enter into a contract with an individual to render services as an independent contractor, provided the subject of the contract is legal according to the Brazilian Civil Law. There are certain activities that should be performed exclusively by professionals duly enrolled in the respective professional council, such as engineers and lawyers, among others.

The contracting party and the independent contractor may freely negotiate the agreement, including terms, fees and other conditions provided the relationship was not established to disguise an employment relationship. The fees must be set and paid in Brazilian currency.

f. Other Ramifications of Classification

There is no prohibition on the use of independent contractors; however, if the elements of the employment relationship are present (services rendered on a personal basis; on a permanent/habitual basis; with subordination, i.e., the services are rendered under the direction of a supervisor; and on an onerous basis, i.e., the individual must receive remuneration in consideration for the services rendered), the independent contractor may be reclassified as an employee.

g. Leased or Seconded Employees

The Brazilian Superior Labor Court has ruled that it is illegal to hire employees through an intermediary. If this is done, an employment relationship will be formed with the intermediary contracting company, except if the employees are temporary workers. Temporary workers in Brazil are regulated by Law 6,019/1974, which provides that temporary workers can be engaged in the following situations:

- to substitute regular employees for a temporary term (i.e during maternity/sick leave); or
- due to a substantial increase in the workload of the company (e.g toy industry over the Christmas period or a company that assumes a new client and will need extra personnel for a specific term to assist with the organization of the documents of such new client).

A temporary worker is hired through a specialized agency, duly registered with the Ministry of Labor. It is a three-party relationship comprising:

- the temporary work agency, (the employer);
- the contracting company (the client); and
- the worker (the temporary employee).

The services agreement for an employee between the client and the temporary work agency cannot exceed three months, except if authorized by the Ministry of Labor, when the agreement may be extended:

- to a maximum of six months in the event of a substantial increase in the workload of the company; and
- to a maximum of nine months as a result of substitution of regular employees for a temporary term

The client will always be secondarily liable for the labor and social security debts of any temporary employee who renders services to the company. Thus, if the temporary worker agency does not comply with the labor and social security law, the client may be held

responsible for such debts.

The temporary worker is entitled to the same remuneration and benefits as the regular employees of the client despite the fact that the temporary employee will be an employee of the agency and not of the client.

The process of outsourcing in Brazil may be unique when compared to other countries. Outsourcing of the core business of a company is not permitted. There is no specific provision of law governing outsourcing, however Precedent 331 of the Superior Labor Court prevails in practically all cases. Secondary activities of a company can be outsourced, for instance cleaning and security activities (for companies which do not have the cleaning and security activities as a core business) and accountancy services (for non accountant companies).

h. Regulations of the Different Categories of Contracts

There are several special regulations applicable to different categories of employees, specifically fixed term employees, part time employees, disabled employees, apprentices, pregnant employees, minimum wages for employed engineers, special conditions for employed drivers, domestic workers, rural workers, airplane crew, offshore activities, journalists, employed soccer players, among others.

Federal laws also regulate different categories of workers who do not act as employees, such as interns/students and commercial sales representatives.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

The re-characterization of an independent contractor as an employee can be determined by a labor court.

In court the independent contractor wishing to establish employee status will need to provide evidence of the four pre-requisites of an employment relationship:

- services rendered on a personal basis;
- on a permanent/habitual basis;
- with subordination; and
- on an onerous basis.

Companies may also be subject to an audit by the Ministry of Labor or social security authorities. Such authorities can assess the existence of an employment relationship and thereafter charge labor and social security contributions.

b. The Legal Consequences of a Re-Characterisation

If an independent contractor is reclassified as an employee, he/she will be entitled to all statutory labor rights described above. The statute of limitations for claiming labor rights in Brazil is five years; however after termination, an employee has only two years from the termination date to file a labor claim.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Individuals can file a labor claim with labor courts, requesting recognition of their employment status and consequent labor rights.

In Brazil, there are courts which specialise in labor matters, so labor courts are competent to rule on any matter arising from or in relation to an employment relationship, including the recognition of an employment relationship.

Filing a labor claim in Brazil is free of charge for employees. The employee has only to declare the impossibility of paying judicial costs in order to be free of all charge, including judicial costs and attorney's fees. A result of the protective nature of the law and free access to Labor Courts, is that the number of labor claims is significant and it is quite common for the larger employers to have several thousand ongoing labor claims at any given time.

Re-characterization of an independent contractor as an employee is a typical labor claim brought by individuals; however it is also possible to have a public civil action dealing with such a matter. Public civil action is a type of lawsuit, similar to a class action, provided for in the Brazilian Federal Constitution. It is the judicial remedy for the protection of collective interests, such as environmental, social and labor issues. Labor public civil actions can be filed by Prosecutors and by several other official entities (i.e. Federal, State and Municipal Governments, Unions, Bar Association, etc.).

In the last few decades, labor public civil actions have become more common and are frequently filed whenever one of the entities mentioned above becomes aware that a particular employer has not complied with labor regulations. Labor Prosecutors can initiate investigations into companies that use independent contractors for the bulk of their workforce.

Labor public civil actions have become a useful tool in ensuring the adherence by employers to all labor regulations and standards. In addition to requesting compliance with the Labor Code and administrative rulings, most of these lawsuits also request collective moral damage indemnifications.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Companies can be audited by the Ministry of Labor, which is in charge of auditing labor obligations, and/or the Federal Tax Revenue, which is in charge of auditing obligations related to social security contributions and income tax.

In the event the Ministry of Labor finds that an independent contractor is in fact an employee, the contracting company may be compelled to pay an administrative fine of approximately BRL 400.00 per employee. This fine will be doubled in the case of relapse.

A Federal Tax Revenue inspection may result in the authorities issuing a notice of infraction requesting the payment of the social security contributions from the previous five years, and an employer may also incur a penalty to the minimum of 75% and maximum of 225% in the case of fraud, and interest based at the SELIC rate.

In both cases, the Labor Prosecutor can be notified and further investigation into the matter initiated.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

The parties should execute a written agreement encompassing the terms and conditions of the relationship (activities, remuneration, place, obligations of both parties, termina-

tion conditions). Such contract should avoid obligations that could imply a subordinate relationship, such as an obligation to report and follow orders, or any sort of economic dependence between the parties. The court will look at the actual circumstances of the relationship and these will prevail over the written agreement.

b. Day-to-Day Management of the Relationship

As already mentioned, in Brazil the actual circumstances of a relationship are more important than formal documents regarding that relationship. Thus, upon hiring an independent contractor and signing a properly written agreement, a company must ensure that it does not interfere in the co-ordination/direction of the independent contractor's activities, does not provide benefits and work tools as if the independent contractor were an employee (corporate cards, uniforms, corporate email, etc.) and does not give personal orders and warnings, etc.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The basic principles of labor relations in Brazil are contained in the Labor Code, "CLT" (Consolidação das Leis do Trabalho), enacted on 1 May 1943. Although it has been altered and amended over the years, the Labor Code is outdated in several respects as it was enacted at a time, which was very different to the social and economic realities of the present day. From time to time, the idea of a major review of the Labor Code is raised at a political level.

Currently, there is a bill of law in the Brazilian Congress, which intends to update various aspects of the Brazilian labor system. It is part of a broader national project to change structural barriers and create a friendlier environment for business. It has been called the "labor reform" and aims at providing enforceability of negotiations with the Union over some matters regulated by law.

We do not foresee, however, significant change in the matter under discussion (employee versus independent contractor). Whenever an independent contractor is treated as an employee, there will be a high risk of reclassification of the independent contractor as an employee.

b. Recent Amendments to the Law

Law 13.352/2016, effective as of 26 January 2017, regulates a partnership relationship between hairdressing salons and stylists, manicurists and other professionals. Despite the constitutionality of this law, it has already been challenged in the Supreme Federal Court and may be used as a parameter for other categories.

VI. CONCLUSION

When determining the best way to hire an individual in Brazil, the company should establish if the relationship it intends to have with the individual would be more likely to be considered an employment or an independent contractor relationship, based on the concrete elements of the actual relationship to be established.

The employment relationship is characterized by four elements, specifically:

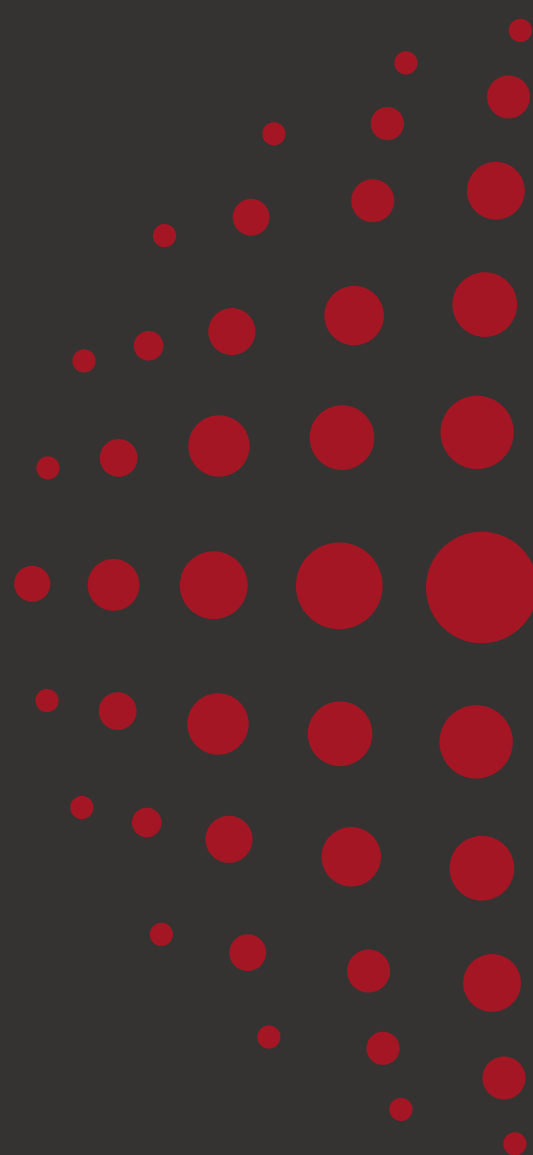
- services rendered on a personal basis;
- with subordination; and
- on an onerous basis.

The independent contractor relationship should not show any characteristic of the employment relationship. Facts prevail over formal documents in Brazil. If the characteristics of an employment relationship are present, the independent contractor may be reclassified as an employee by labor courts even if a worker is hired as an independent contractor.

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CANADA

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I. OVERVIEW

a. Introduction

In Canada, companies have increasingly sought to classify workers as independent contractors in an attempt to reduce costs and administrative obligations. Workers generally do not oppose this classification as a result of favourable tax treatment enjoyed by contractors and other small businesses.

Unfortunately, most independent contractors in Canada are misclassified and many would be deemed employees if the arrangement between them and the company retaining their services was reviewed by a governmental authority or court. Often, such a review occurs when a worker has the contract arrangement terminated and seeks employment termination or employment insurance benefits.

Misclassification of workers can have profound consequences for both the company and the wrongly classified worker. Accordingly, the importance of understanding the classification of workers as employees or contractors has increased in recent years.

Classifying a worker as an employee or an independent contractor in Canada involves a complex assessment of the true nature of the working relationship. Courts and adjudicators have established a complicated and flexible analysis for making such a determination. The importance of making a correct classification cannot be understated. It is hoped that the following will assist companies and workers in making proper classification decisions and avoiding the financial liability associated with misclassification.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Determining whether an individual is an employee or an independent contractor under Canadian law is more of an art than a science. In simple terms, actions speak louder than words. A well-drafted and properly executed contract will not be determinative in evaluating the status of the relationship between the individual in question and the company retaining his or her services.

In making status determinations, Canadian courts and administrative tribunals will consider the subjective intention of the parties, which may include a written contract, along with the objective reality of the working relationship. The weight that Canadian courts and tribunals place on a written contract varies.

In a recent decision, the Federal Court of Appeal restated the legal test applicable to determining whether an individual is an employee or an independent contractor¹. The current test articulated by the Federal Court of Appeal is encapsulated by the following two-step inquiry:

- first, the court should determine the subjective intention of the parties by written agreement or conduct; and
- second, the court should ascertain the objective reality by evaluating whether the facts are consistent with the parties' stated intentions.

¹ 1392644 Ontario Inc. (Connor Homes) v Canada (National Revenue), 2013 FCA 85 (“Connor Homes”).

In addressing the second step, decision-makers will often consider the following four factors enunciated in the case of *“Wiebe Door”*, (frequently referred to as the *“Wiebe Door”* factors):

- control
- ownership of Tools
- chance of profit
- risk of loss²

The courts have repeatedly held that no particular factor is dominant.³ Instead, these four factors constitute a non-exhaustive list, and there is no set formula as to their application. The relative weight of each factor will depend on the particular facts and circumstances of each case.⁴ In this respect, the courts will consider all factors, and will evaluate the totality of the relationship on a case-by-case basis. In applying the *Wiebe Door* factors, the courts will consider some or all of the following questions for each factor:

Control

Is the worker under the direction and control of another regarding the time, place, and manner in which the work is performed? Is the worker hired, given instruction, supervised, controlled, or subject to discipline? Does the worker set his or her own hours and complete work independently? Can the worker hire subcontractors to complete the work? Arrangements whereby the worker is given greater flexibility over how and when the work is performed tend to suggest an independent contractor relationship.

Ownership of Tools

Does the worker use tools, space, supplies or equipment provided by the company or does the worker utilize his or her own resources to complete the work? Arrangements whereby the worker supplies his or her own highly specialized and/or expensive equipment may suggest a non-employment relationship. Arrangements whereby the company supplies most of the resources may suggest an employment relationship.

Chance of Profit

Can the worker increase his or her earnings by using entrepreneurial skills? Is the worker paid an hourly rate, which limits his or her chance of profit, or is he or she paid piecemeal, meaning greater efficiency may increase profits? Arrangements whereby a worker's skills, efficiency, or entrepreneurial work can increase the worker's earnings tend to suggest an independent contractor relationship.

Risk of Loss

Is the worker at risk of losing money if the cost of doing a job is more than the price charged for it? Is the worker at risk of not being paid if the work is not done correctly? Arrangements whereby workers are at a greater risk of loss when performing services may favour a finding of a non-employment relationship.

In considering the above, it is clear the courts will consider status issues on a case-by-case basis by evaluating all relevant facts and circumstances. A contract will not ensure a particular status if the practical reality is not consistent with that status. To make matters more complicated, a determination in one forum may not always be binding in another.

For instance, a finding in the Tax Court of Canada (the “Tax Court”) that an individual is an independent contractor may not result in the same finding under employment standards

² These factors were enunciated in *Wiebe Door Services Ltd v The Minister of National Revenue* (1986), 87 DTC 5025 (Fed CA) (*“Wiebe Door”*) and *671122 Ontario Ltd v Sagaz Industries Canada Inc.*, [2001] 2 SCR 983 (*“Sagaz”*).

³ See for instance *Wiebe Door* and *Sagaz*.

⁴ See *Sagaz*, supra at para 48. Risk of Loss

legislation. Indeed, despite the importance of correctly characterizing an employment relationship, there is no universal definition of “employee” in Canadian legislation. The Supreme Court of Canada has stated that when courts and tribunals are examining whether or not a particular individual is an “employee”, the particular policy objectives of the statute at issue must be taken into account.⁵

b. General Differences in Tax Treatment

There are many tax advantages for both companies and individuals in classifying workers as independent contractors rather than employees.

For companies, payment will be made directly to the independent contractor, without any required source deductions. Also, companies will not be required to make deductions or employer contributions to various government programs, namely, for Employment Insurance (“EI”) or the Canada Pension Plan (“CPP”) premiums.

For the independent contractor, the lack of deductions means more money in his or her pocket. The totality of income tax and premium deductions can be significant, so the independent contractor benefits greatly from reducing and deferring the income tax payable, and from never having to make EI or CPP contributions unless he or she qualifies for, and opts into, a corresponding program.

Independent contractor status also provides the independent contractor with other tax advantages. Independent contractors can write off various business expenses, which may include home-related expenses such as internet, phone, utilities, and even a portion of mortgage/housing rental fees, along with business equipment, business use vehicles, gas, meals, and sometimes entertainment. This means that the independent contractor has the potential to net far higher earnings than an employee earning a similar gross amount.

The possibility of savings for the company does not come without risk. A company can face significant liabilities if the Canada Revenue Agency (“CRA”) determines that an individual who has been treated as an independent contractor is actually an employee. Such liabilities may be of particular concern to businesses that classify a significant portion of their workers as independent contractors (for instance, as may be seen in a taxi or tow-truck company). A reassessment in those cases could compromise the future of the business. As such, companies that contract with a significant number of independent contractors should ensure that a well-drafted independent contractor agreement for each worker is in place, and that the practical reality of the working relationship is consistent with the worker's designation as an independent contractor. Otherwise, a moderate tax advantage today could become a far greater tax liability tomorrow, as the reassessment of a worker's status could mean that the company would be responsible not only for its own premiums and deductions, but also the worker's portion that it failed to remit.

In this respect, there may be advantages to classifying a working relationship as employer-employee. Deductions are made by the employer, without potential liabilities relating to income tax, EI and CPP. An employer-employee classification also provides increased protection for the worker, including the ability to apply for EI benefits should he or she become unemployed.

c. Differences in Benefit Entitlement

In general terms, independent contractor status provides workers with financial/tax

⁵ *Pointe Claire v SEPB*, [1997] 1 SCR 1015.

benefits (as described above) at the cost of all other employment-related benefits. For instance, given that independent contractors are not required to pay government premiums for EI or CPP, they likewise will not qualify for receipt of these benefits. In this respect, an independent contractor will not receive government income protection (EI) for a period where they do not have work. Also, they will not receive government pension payments by way of CPP benefits, unless they elect to contribute.

Further, independent contractors are not entitled to the basic protections of employment standards legislation. This includes the benefit of vacation pay and statutory holiday pay. Employees protected by employment standards legislation are also entitled to take various paid leaves of absence, including, but not limited to, pregnancy leave, parental leave, sick leave, and family medical leave. Independent contractors have no such entitlement.

In terms of medical benefit coverage, Canada's employment standards legislation generally does not require that companies provide medical insurance benefits for employees; however, medical benefits are often provided to employees as part of a negotiated remuneration plan. It is unlikely that an independent contractor would receive medical benefit coverage, which may include provisions for long-term disability, extended health, dental, and other insurance coverage. Notably, Canadians have universal health care coverage and are not required to pay directly for most non-elective medical procedures and assessments.

Canadian jurisdictions feature workplace safety and insurance regimes to provide benefits coverage in the event of a work-related accident. Such coverage may include loss of earnings payments, medical treatment coverage, and even retraining for a new career. Generally, while employees qualify for such coverage, independent contractors do not.

There may be special status for independent contractors in various workplace safety and insurance regimes. For instance, in Ontario, individuals can apply for optional insurance for "independent operators". Not only does this benefit the contractor (aka the operator), but it also provides significant legal protection to the company, as workers entitled to benefits under the Ontario Workplace Safety and Insurance Act for work-related injuries are generally precluded from pursuing civil actions (i.e. personal injury lawsuits) to recover damages for work-related injuries. In contrast, an independent operator without optional coverage may be free to sue the company for damages in respect of a work-related injury.

d. Differences in Protection from Termination

Both independent contractor and employment relationships can be terminated; a key distinction between them as to termination involves entitlement to notice of termination.

Independent contractors are generally not entitled to notice of termination under employment standards legislation or the common law, unless their contract contains a provision that stipulates some form of notice.

Generally, employees are entitled to notice of termination. First, applicable employment standards legislation sets minimum requirements for notice and, depending on the jurisdiction, severance pay. Second, employees may also be entitled to common law reasonable notice of termination, unless a contract of employment otherwise limits notice. Reasonable notice at common law is a remedy that the courts can provide for employees terminated without notice or insufficient notice, which is more often than not far greater than the minimum statutory requirements. An employee is entitled to at least the minimum legislative standards in respect of notice and severance, if applicable,

except in the case of significant misconduct (often termed as "just cause").

Some Canadian courts have recognized an intermediate category of contractor, between an employee and an independent contractor. This intermediate category is often referred to as a "dependent contractor" because it is economically dependent on the contracting company. A dependent contractor will generally be entitled to notice of the termination of his or her contract, however, the amount of notice to which a dependent contractor will be entitled at common law is less than the amount of notice to which a similarly-situated employee would be entitled.⁶

Notably, most of the law considering status disputes has evolved out of the Tax Court; however, other adjudicators consistently consider the Wiebe Door factors and generally apply an analogous approach.

Often such cases only come forward at the end of a relationship where a former worker, classified as an independent contractor, becomes dissatisfied with the notice of termination received when the relationship ceases. Unfortunately, even though that individual may have reaped the tax benefits of independent contractor status for years, he or she may be considered an employee or dependent contractor under the above tests, and thus, be entitled to reasonable notice of termination.

e. Local Limitations on Use of Independent Contractors

The main limitation on the use of independent contractors in Canada is the risk that they will be reclassified as employees. As discussed above, an employer could face substantial legal liability if an independent contractor is found to be an employee.

Another limitation relates to work performed under a collective agreement. Where, pursuant to a collective agreement, a union holds the bargaining rights for a particular class of workers, it may be a violation of the collective agreement for the company to hire independent contractors to complete the work ordinarily conducted by workers in the bargaining unit. A company cannot circumvent a union's bargaining rights by assigning bargaining unit work to independent contractors where the collective agreement so provides.

f. Other Ramifications of Classification

Labour Relations Ramifications

Pursuant to provincial labour legislation, such as the Ontario Labour Relations Act, where an individual is considered an "employee", that individual may be included as part of an existing bargaining unit, or may be eligible to be included in an application for certification of a union. Under the Labour Relations Act, only employees, which, by statutory definition, includes "dependent contractors", are eligible to unionize and collectively bargain. Independent contractors would therefore not be eligible to participate in the collective bargaining regime.

Insolvency Ramifications

If a company becomes insolvent, whether a worker is an independent contractor or an employee can affect the priority for amounts to be paid to the worker. Pursuant to the federal Bankruptcy and Insolvency Act, as well as various other statutes, employees take priority over other creditors up to certain amounts. By contrast, independent contractors do not have the same priority.

⁶ McKee v Reid's Heritage Homes Ltd., 2009 ONCA 916

g. Leased or Seconded Employees

Use of a staffing agency may provide more flexibility to meet a company's staffing needs. The use of an agency may limit various liabilities, including those arising from wrongful dismissal claims. Further, the contracting company will not be required to pay premiums for EI, CPP or other employment-related benefits in respect of agency employees. However, these costs savings may factor into the fee charged by the agency.

In the event that a company contracts with or seconds employees from an agency or another company, the company should ensure that an arms-length relationship with these employees is preserved by the practical realities of the engagement. For instance, if the company controls all aspects of the work, it may be found to be the "true employer" of the agency employees, which could result in liability for various employment-related matters.

Further, even contracting with workers from an agency may not limit liabilities in certain legal venues. For instance, the contracting company may, in some circumstances, have all or at least partial liability in respect of a workplace accident. Further, a contractor could file a human rights application against the contracting firm. As such, while using an agency does provide some protection, these protections are not boundless. Given the practical realities of working relationships, a contractual relationship may be most useful for fixed-term work projects or temporary work.

h. Regulations of the Different Categories of Contracts

Employment agreements in Canada are regulated only in the sense that a court or government body (such as the CRA) can review or analyze a relationship in the course of litigation, at the request of one of the parties, or in some cases, by undertaking an independent audit. Otherwise, parties are generally free to enter into whatever sort of relationship they wish, provided they comply with the statutory requirements that arise depending on how the relationship is classified. The relationship between the parties who enter into an agreement is generally regulated by that agreement, and will not be subject to judicial or administrative review, unless a dispute arises that results in litigation.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

It is crucial that parties clearly define whether or not they have an employer-employee or an independent contractor relationship. Nevertheless, simply labelling a worker an "employee" or an "independent contractor" is not sufficient to establish such a relationship. The intention of the parties is but one of many factors that will determine how the relationship is ultimately viewed. Rather, the total relationship between the parties will be examined.

In engaging in such review, courts and adjudicators will consider the Wiebe Door factors noted above. Courts will also review the degree of economic independence in the employment relationship (that is, whether a party is carrying on business for himself/herself or on behalf of a superior). The duration of the relationship between a worker and a company is also an important factor. If an independent contractor has been providing services to a company for many years, is providing little (or no) services to other companies, and has become dependent upon the company for income, this may indicate that the worker is a dependent contractor or an employee rather than an independent contractor.

Such tests are open to a great deal of interpretation, and the aforementioned factors are not exhaustive. However, they are important considerations that will be looked at in examining the status of an employment relationship.

b. The Legal Consequences of a Re-Characterisation

The issue of whether an individual is an employee or an independent contractor is significant because an individual's status as an employee will trigger the application of a variety of statutory rights and benefits under a number of pieces of legislation.

In Ontario, for instance, employers' specific obligations to employees may arise under the following statutes: the *Income Tax Act*, the *Employment Insurance Act*, the *Canada Pension Plan*, the *Employment Standards Act*, the *Workplace Safety and Insurance Act*, the *Pay Equity Act* and the *Labour Relations Act*.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The remedies available to those seeking employee status depend on the forum in which the status is sought.

Pursuant to the *Employment Insurance Act*⁷ and the Canada Pension Plan⁸, workers may apply to the CRA for a determination of their status. A ruling will determine whether a worker is "self-employed" (i.e. an independent contractor) or an "employee", and thus, whether that worker's employment is pensionable or insurable under the *Canada Pension Plan* and/or the *Employment Insurance Act*. If an individual is found to be an employee by the CRA or the Tax Court, he or she may be eligible for EI or CPP benefits.

Further, an individual who has been found to be an employee may be entitled to damages for wrongful dismissal (i.e. common law notice) in the courts.

In other cases, newly reclassified employees may choose to file an employment standards claim to seek remedies under employment standards legislation, such as notice and severance pay, vacation pay, public holiday pay and/or overtime pay.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Mischaracterization of the relationship between an employer and a worker can result in liability for the employer under a number of statutes.

Tax Implications

Employers are obligated to deduct employment income at source from all employees for tax remittance purposes. Such deductions are not required for independent contractors. Where an independent contractor is subsequently deemed to be an employee, the employer may be liable for the deductions that should have been made from the worker's income. When this occurs, the CRA generally will first turn to the individual for the outstanding amounts; however, the employer will remain liable if the individual is unable to pay, or cannot be located. The CRA can assess a penalty of 10 percent of the amount of CPP, EI, and income tax an employer fails to deduct, and can apply up to a 20 percent penalty to a second or later failure to deduct in the same calendar year, if such failure was made knowingly or by gross negligence.

⁷ Canada Pension Plan, RSC 1985, c C-8 at section 26.1.

⁸ Employment Insurance Act, SC 1996, c 23 at section 90.

Pensions and Insurance Implications

CPP payments and EI benefits are both administered by the CRA. The same factors used to determine whether an individual is an “employee” for income tax purposes are also considered in determining whether an individual is an employee or an independent contractor for the purposes of the application of both the *Employment Insurance Act* and the *Canada Pension Plan*. For both CPP and EI, employers are required to make an employer’s contribution, and to deduct the employee’s contribution to remit to the CRA.

With respect to CPP, employers are not expected to make contributions for independent contractors. An employer who fails to deduct required CPP contributions from an employee has to pay both the employer’s share and the employee’s share of any premiums owing, plus penalties and interest. Therefore, where an individual who has been operating as an independent contractor is deemed to be an employee, there are significant financial repercussions for the employer.

With respect to EI, independent contractors do not receive benefits, and no contributions are required. However, it is not unusual for independent contractors to dispute their status as independent contractors after their contract is terminated. If it is determined that they were, in fact, employees, they will be eligible for EI benefits. In such circumstances, an employer may be liable for the payment of both the employee’s and the employer’s contribution for a period that includes the current year, and up to the three previous years, including interest and penalties.

The current prescribed interest rate (as of September 20, 2016) for unremitted income tax, CPP, and EI contributions is 5 percent, compounded daily. Interest applies to the penalties described above as well.

Workplace Safety and Insurance Act Implications

Pursuant to provincial workers’ compensation legislation, such as Ontario’s *Workplace Safety and Insurance Act* (the “*WSIA*”), certain individuals are entitled to benefits if they are injured while at work. Whether or not a specific individual is covered under the *WSIA* (and is thus eligible for benefits) frequently will depend upon whether that worker is considered an “independent operator” or a “worker”. Workers, defined under the *WSIA* to include any person who “has entered into or is employed under a contract of service”, are generally entitled to benefits if they are injured at work. In contrast, so-called “independent operators”, or those working under contracts for services, may not be entitled to benefits under the *WSIA*, unless they voluntarily apply to the Workplace Safety and Insurance Board (the “*WSIB*”) for optional insurance coverage.⁹

Workers may file a complaint with the *WSIB* against employers who do not fulfill their obligation to pay benefit contributions. In addition, the *WSIB* may audit employers to ensure that premiums are being paid on behalf of all workers. The *WSIB* has broad powers of enforcement. If an employer fails to pay the premiums in respect of a worker, the employer may be ordered to pay the amount of premiums payable for one year, and as a penalty, may be ordered to pay that amount again.¹⁰ Employers may also be liable to a worker for any losses suffered by that worker as a result of the employer’s non-compliance. As such, if an individual is injured and it is determined that they are, in fact, an employee and not an independent operator, then there may be serious implications for the employer.

Wrongful Dismissal Claims

Generally, independent contractors cannot claim damages for wrongful dismissal; however, if a court finds that an alleged independent contractor was actually an employee or a dependent contractor, that individual may be entitled to reasonable

notice of termination at common law or payment in lieu thereof.

As noted above, employment status issues in wrongful dismissal claims commonly arise following the dismissal of a worker who has been functioning as an independent contractor for the duration of his or her tenure with the Company. When that independent contractor realizes, for instance, that he or she is not receiving a severance package, the independent contractor may claim that he or she was actually an employee and thus should have received reasonable notice at common law.

The length of the reasonable notice period owing to an employee will depend upon a number of factors, including the age of the employee, his or her length of service, the position he or she held when he or she was terminated, and the availability of alternate employment. As stated above, dependent contractors will generally be entitled to less notice than employees.

Vicarious Liability of Employers

In general, an employer is vicariously liable for the acts and omissions of an employee where such acts or omissions are committed by the employee “in the course of employment”. By contrast, employers generally are not vicariously liable for the actions of an independent contractor. If an independent contractor is found to actually be an employee, the employer may then be liable for the acts and omissions of that individual.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Before engaging the services of a worker, an employer should first and foremost consider what relationship it wishes to establish with the worker. The employer should then draft a written agreement that reflects the Wiebe Door factors. Employers who wish to enter into an independent contractor relationship with a worker would be wise to structure the relationship in such a way as to include as many factors indicative of an independent contractor arrangement, and to exclude as many factors indicative of an employment arrangement, as possible. The terms of the relationship should be clearly set out in a written agreement that explicitly states what type of relationship the parties wish to enter into. In the case of an independent contractor, the agreement should be titled “Independent Contractor Agreement” or “Contract for Services” (as opposed to a “Contract of Service”). As previously mentioned, a written agreement between the parties will not be determinative of the relationship, but will nevertheless play a role in establishing the nature of that relationship.

The agreement should also include legally enforceable termination provisions. It may be prudent to limit the independent contractor’s entitlement on termination to the minimums set out in applicable employment standards legislation, to mitigate the risk that an independent contractor may be found to be an employee.

Both the employer and the worker must act within the relationship described in their written agreement. In the event a relationship is assessed, it will not be helpful if the agreement between the parties is titled “Independent Contractor Agreement”, but the parties are behaving as though the relationship is one of employer-employee. The bottom line is, if an employer wishes for an adjudicator to treat its relationship with a worker as an independent contractor relationship, the employer should give the worker as much independence as is reasonably possible, and should treat the worker almost as though he or she were a separate business entity.

⁹ Workplace Safety and Insurance Act, SO 1997, c 16, Sched A at section 12

¹⁰ Ibid at section 88(5).

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The trend in Canada in recent years, much like the trend elsewhere, has moved towards an increased use of independent contractors and short-term contracts. In Canada, this has led to a corresponding increase in the frequency of litigation at the Tax Court of Canada, as a greater number of workers classified as independent contractors are seeking entitlement to benefits only enjoyed by employees.¹¹ Consequently, issues pertaining to employment status have taken on more significance than ever before.

In at least one Canadian jurisdiction, the effect of the increased level of independent contractors has been studied to determine the effect on employees and on workplaces. In 2015, the Ontario Ministry of Labour commenced a “Changing Workplaces Review” to determine whether the current employment and labour legislative schemes need to be amended to reflect Ontario’s and Canada’s changing workplaces. The Ministry appointed two Special Advisors to study Ontario workplaces, and to devise recommendations to bring the legislation in line with current practices. On July 27, 2016, the Special Advisors issued a report based on public consultations and submissions. The report made a large number of recommendations relating to a variety of employment issues for public consideration. One set of recommendations pertains to the proliferation of independent contractors and a corresponding increase in the number of misclassified workers. The report found that the number of employees who were misclassified as independent contractors was increasing and that the legislation needs to respond to this growing area of concern. The Special Advisors’ recommendations to rectify the issue included: (i) an added burden on employers to prove that a person is correctly classified as an “independent contractor” when a dispute arises; (ii) an increase in the proactive education of workers so that they can determine whether they are employees themselves; and (iii) the inclusion of “dependent contractors” within the definition of “employee” under provincial employment legislation.

At this point in time, it is unclear whether the Special Advisors’ recommendations will gain traction in Ontario or elsewhere in Canada, but if adopted, they could have a significant impact on Canadian workplaces. It will be important to monitor any relevant legislative developments, and to monitor other Canadian jurisdictions to see if any others follow suit. A change in one province may signal a larger scale change on the horizon, which would have significant implications for Canadian legal practitioners, companies, and workers.

b. Recent Amendments to the Law

Generally speaking, the law pertaining to the classification of workers as contractors or employees has not changed significantly in recent years. Canadian Courts have consistently demonstrated a willingness to adopt the Wiebe Door factors in assessing how workers should be classified. Canadian Courts have also demonstrated a willingness to elaborate on the Wiebe Door factors by adding other factors to consider, and by commenting further on the third classification category, namely, the dependent contractor category.

Stated Intent of the Parties

Canadian courts have taken varying approaches with respect to the weight that should be given to written contracts in making status determinations. For instance, some decisions heavily favour a finding consistent with the written contract agreed to by the parties, while other decisions completely ignore the same.

¹¹ See *Big Bird Truck Inc. v. Minister of National Revenue*, 2015 TCC 340

Royal Winnipeg Ballet v MNR (2006 FCA 87) (“*Winnipeg Ballet*”) suggests that substantial weight should be given to the stated intention of the parties. In *Winnipeg Ballet*, the Federal Court of Appeal overturned a previous decision by the Tax Court, which had found that three dancers were employees and not independent contractors.

The evidence clearly indicated that both parties understood the dancers to be independent contractors, and that the parties acted in a manner consistent with this understanding. The dancers charged a Goods and Service Tax (GST) for their services, and the employer did not withhold taxes. The agreement contained no express provision regarding the dancers’ status. It set out, *inter alia*, minimum rates of pay, contributions to health care, and disability insurance. Dancers were required to pay for certain costs independently, including costs relating to rehearsal outfits and makeup, while the employer was required to pay for other costs, such as the purchase of costumes.

The majority of the Federal Court of Appeal held that “in determining the legal nature of a contract, it is a search for the common intention of the parties that is the object of the exercise”.¹² The Federal Court of Appeal found that the Tax Court erred in failing to consider the parties’ intention, and should have considered the Wiebe Door factors in light of the evidence that both parties had understood and acted as though the dancers were independent contractors. The Federal Court of Appeal acknowledged that the understanding of the parties with respect to status is not necessarily determinative, and noted that if the parties’ stated intention is not reflected in the terms of the applicable contract and the practical reality of the day-to-day relationship in dispute, then the parties’ intention will be disregarded.

The *Winnipeg Ballet* decision has been applied with varying results in subsequent decisions. In considering this varying jurisprudence, the Federal Court of Appeal in *Connor Homes* (discussed above) recently clarified the test to be applied in determining the status of a worker, as outlined above. Specifically, at paragraphs 39 to 41 of *Connor Homes*, the Court endorsed the following two-step inquiry:

Under the first step, the subjective intent of each party to the relationship must be ascertained. This can be determined either by the written contractual relationship the parties have entered into or by the actual behaviour of each party, such as invoices for services rendered, registration for GST purposes and income tax filings as an independent contractor.

The second step is to ascertain whether an objective reality sustains the subjective intent of the parties. As noted by Sharlow J.A. in *TBT Personnel Services Inc. v. Canada*, 2011 FCA 256, 422 N.R. 366 at para. 9, “it is also necessary to consider the Wiebe Door factors to determine whether the facts are consistent with the parties’ expressed intention.” In other words, the subjective intent of the parties cannot trump the reality of the relationship as ascertained through objective facts. In this second step, the parties’ intent as well as the terms of the contract may also be taken into account since they color the relationship. As noted in *Royal Winnipeg Ballet* at para. 64, the relevant factors must be considered “in the light of” the parties’ intent. However, that being stated, the second step is an analysis of the pertinent facts for the purpose of determining whether the test set out in *Wiebe Door* and *Sagaz* has been in fact met, i.e. whether the legal effect of the relationship the parties have established is one of independent contractor or of employer-employee.

The central question at issue remains whether the person who has been engaged to perform the services is, in actual fact, performing them as a person in business

¹² *Royal Winnipeg Ballet v MNR*, 2006 FCA 87 at para. 59.

on his own account.¹³

Recent jurisprudence appears to adopt the reasoning set out in *Winnipeg Ballet and Connor Homes* and appears to support the proposition that the intention of the parties is a factor to be considered¹⁴. That said, it remains to be seen what weight adjudicators will ascribe to this factor relative to others in the future.

Dependence on the Employer

The Ontario Court of Appeal considered the differences between employees, dependent contractors and independent contractors in *McKee v Reid's Heritage Homes Ltd*, 2009 ONCA 916. The plaintiff in that case carried on business through her company and even engaged her own employees. Her contract, although no longer binding, seemed to demonstrate an intention that she be considered a contractor. The plaintiff was paid by commission; however, she was economically dependent on the defendant company, as she had worked exclusively for the defendant for a number of years.

The Ontario Court of Appeal considered a number of factors, including the following:

- whether the person works exclusively for the employer;
- whether the person is subject to the control of the employer;
- whether the person owns the tools of the trade;
- whether the person has undertaken risk or loss/chance of profits, as distinct from fixed compensation; and
- whose business is it?

The Court concluded that the plaintiff was an employee rather than an independent contractor or a dependent contractor. Accordingly, the plaintiff was entitled to reasonable notice of the termination of her contract.

This case demonstrates that if the worker is in an economically vulnerable position vis-a-vis an employer, there is a risk that a court will find that an employment relationship or a dependent contractor relationship exists. This decision is also notable because it sheds greater light on the intermediate “dependent contractor” category. A dependent contractor is dependent on the employer for most or all of his or her business. Dependent contractors are entitled to notice of termination, although not to the same extent as employees.

As the concept of the dependent contractor category has only relatively recently been adopted by Canadian courts, it will be interesting to see how the jurisprudence in this area continues to evolve, and how courts will endeavor to strike a balance between employees and independent contractors in the future.

Status Quo in the Legislation

It should be emphasized that the case law pertaining to employee classification is largely settled, and has not undergone significant change in recent years. The same can also be said of the applicable statutory regime. The statutes discussed above, including the *Employment Insurance Act*, the *Canada Pension Plan*, and the *Income Tax Act*, have not been significantly amended as they relate to independent contractors. The legislation's application to independent contractors is minimal, especially compared to the degree to which provision is made for employees. It appears that Canadian legislators are satisfied with the status quo, and that they are satisfied with the minimal application to independent contractors.

As discussed above, it may be interesting to monitor legislative developments at both

¹³ Supra note 1 at paras 39-41.

¹⁴ See *Porotti v. Minister of National Revenue*, 2016 FCA 29.

the federal and the provincial level to determine whether dependent contractors are brought within the scope of the applicable statutes. It may be reasonable to speculate that dependent contractors will eventually be brought within the application of a broad range of employment-related legislation, such that they will be entitled to the same or similar benefits as employees.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

Generally speaking, a non-resident corporation that carries on business in Canada will be subject to Canadian tax filing requirements and will be required to pay taxes on business profits attributable to that establishment.¹⁵ However, it is worth noting that Canada is a party to the Convention between Canada and the United States of America with Respect to Taxes on Income and on Capital (the “Convention”), which may alter the foregoing default arrangement. Article VII of the Convention provides that business profits will only be taxable in Canada if the non-resident carries on business through a “permanent establishment”. Article V establishes two types of permanent establishments: a “fixed place of business” or a “dependent agent”. A dependent agent must have the authority, and must habitually exercise that authority, to conclude contracts in the name of the U.S. corporation. Paragraph 7 of Article V stipulates that a permanent establishment will not be created where business is carried out in Canada through a broker, general commission agent, or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

The following key factors in the dependent agent permanent establishment analysis are set out in *American Income Life Insurance Co. v Canada*, 2008 TCC 206 (“*American Income*”):

- did the agent have the authority to conclude contracts in Canada?
- was the agent of independent status, both legally and economically?
- was the agent acting in the ordinary course of his or her business?

With respect to permanent establishment, the CRA's views are generally consistent with those of the Organization for Economic Co-operation and Development (“OECD”) in its Model Tax Convention on Income and on Capital and its Commentary. The OECD has clarified that a dependent agent must habitually exercise its authority to conclude contracts, and that those contracts must relate to the operations that constitute the “business proper” of the non-resident.

In light of the foregoing, a truly economically independent contractor in business for him or herself is unlikely to create a permanent establishment for the purposes of Canada's *Income Tax Act*. The independent contractor versus employee tests outlined above will be relevant in determining whether an agent was performing services as a person in business on his or her own account. If the agent was not in business for him or herself, then that agent must have significant contracting authority in order to create a permanent establishment.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

The employment of one or more individuals in Canada may create a permanent establishment where there is either a fixed place of business, or where business is

¹⁵ *Income Tax Act*, RSC 1985, c 1 (5th Supp.), at section 2(3)(b).

conducted via a dependent agent. The ramifications of the creation of a permanent establishment include that the non-resident corporation will be required to pay taxes in Canada on its business profits attributable to the permanent establishment.

An employee in Canada may create a permanent establishment where that employee has significant power to bind the non-resident corporation in contract. Such authority must extend to concluding contracts relating to the operations that constitute the “business proper” of the non-resident, and this authority must be exercised habitually. Whether an employee’s contractual authority will be sufficient to create a permanent establishment will depend upon the particular facts and circumstances of each case.

VII. CONCLUSION

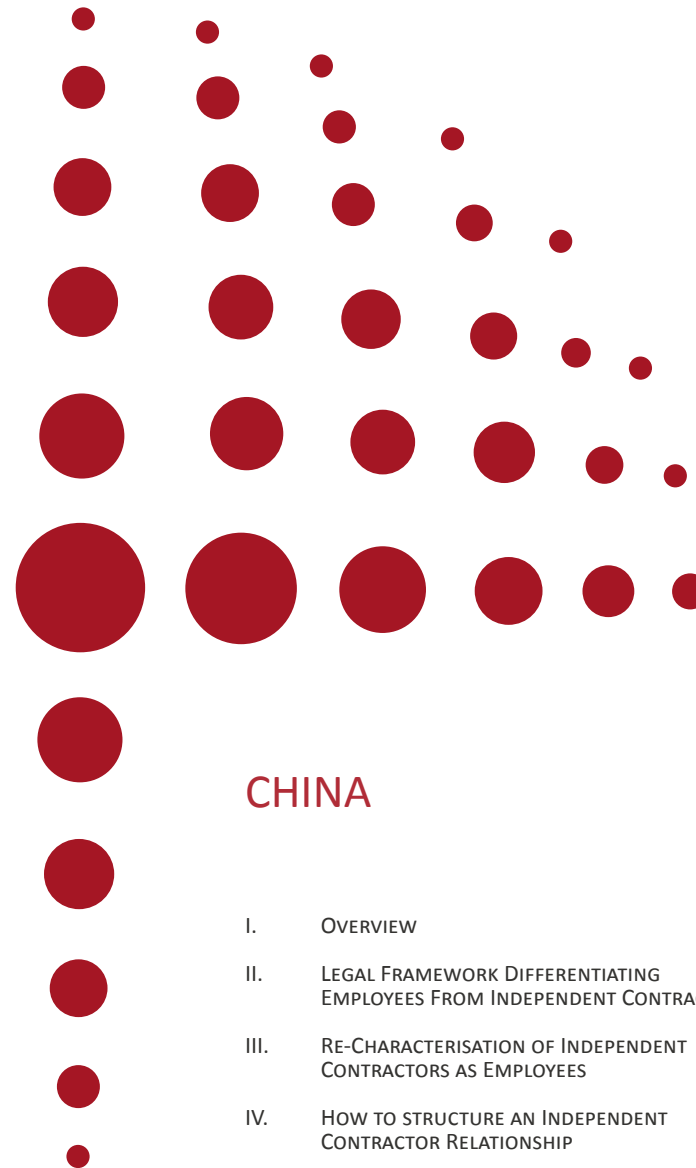
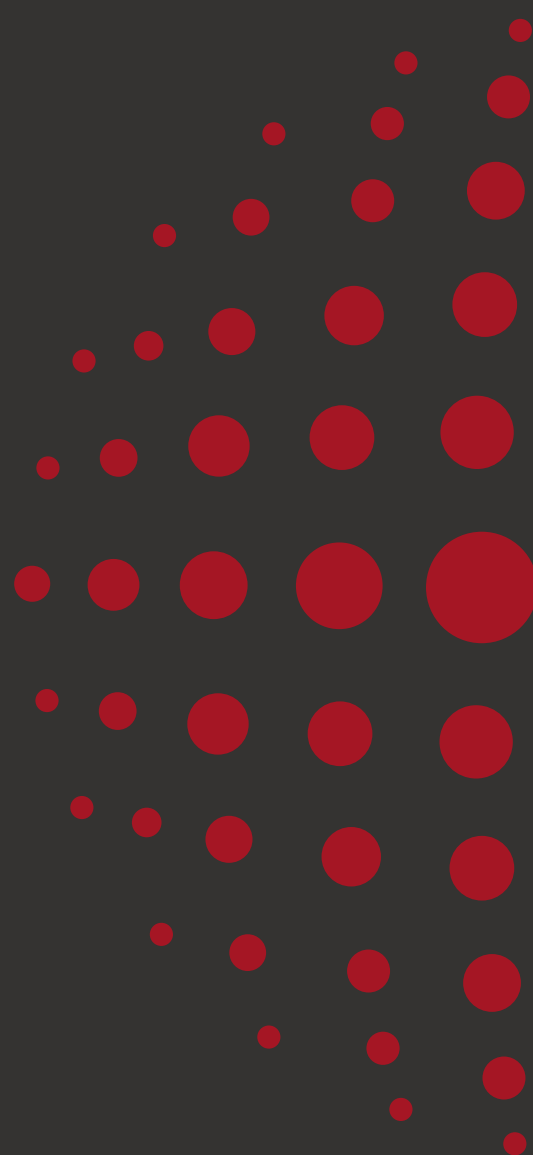
The foregoing summarizes some of the distinctions between employees and independent contractors in Canadian law.

In Canada, the line between who is an employee and who is an independent contractor is often blurred, which may have significant implications for employers. If an independent contractor is found to be an employee, the employer faces significant liability under a number of statutes, as well as under the common law. Consequently, it is imperative that the relationships between workers and the companies retaining their services be both correctly characterized under clear and legally enforceable written agreements, and correspond to practical realities that are consistent with those agreements.

Generally, the factors applied by Canadian adjudicators in assessing the status of a worker will examine the totality and true nature of the relationship in dispute. In simple terms, if an individual looks like an employee and acts like an employee, adjudicators in Canada are likely to find that he or she is in fact an employee.

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CHINA

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I. OVERVIEW

a. Introduction

According to the Labor Laws of the People's Republic of China, "employees" could be generally defined as the individuals who have established employment relationships with the businesses or individual economic organizations (hereinafter referred to as "employers") within the territory of the People's Republic of China or who have contractual employment relationships with the government organs, institutions or social organisations. Therefore, whether an individual is an employee depends on whether there is an "employment relationship" between the individual and the employer.

On the other hand, there is no specific concept of "independent contractor" under the labor laws of China, but under the civil laws of China, an individual may enter into a contract for service with a company or business under certain conditions, and both parties of the contract are equal and independent civil subjects without subordinate relationships. Such individual is referred to as an "independent contractor" for the purpose of the discussion in this article. In practice, the question whether a person is an employee or an independent contractor usually comes up when the company engages an unretired person and enters into a contract for service instead of an employment contract with the person. In this case, the contract for service would be easily confused with the employment contract for an employee. If any dispute arises from or in connection with the contract for service, the person will likely initiate labor arbitration and litigation proceedings to request confirmation of the employment relationship. If the effective arbitration award or judgment finally confirms that the person has an employment relationship with the company, this person should be an "employee" and will be entitled to protection by labor laws. Otherwise he/she would generally be deemed an "independent contractor".

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

In practice, labor arbitration commissions and courts mainly refer to the Circular of the Ministry of Labor and Social Security on the Establishment of Employment Relationship (hereinafter referred to the "Circular") to determine whether an employment relationship exists. According to the Circular, the basic characteristics of an employment relationship are: (1) both the employer and the employee are qualified to enter into an employment relationship according to law; (2) the employer's various rules and regulations formulated in accordance with the law are applicable to the employee, and the employee is subject to the employer's labor management and is engaged in certain paid work arranged by the employer; and (3) the employee's work is part of the employer's business. If the three factors above are satisfied simultaneously, an employment relationship shall be deemed to have been established, and the person involved should be an employee instead of an independent contractor.

Also, the Circular further provides that the following vouchers could be used as reference for confirmation of the employment relationship between two parties when there is no written employment contract: (1) wage payment voucher or record (employee payroll) and the record of various social insurance contributions; (2) the certificates such as the "Work Certificate" and the "Service Certificate" that can prove the identities issued by the employer to the employee; (3) the recruitment and employment records of the employer such as the "Registration Form" and the "Enrolment Form" that have been filled in by the employee; (4) attendance records; and (5) testimony of other employees.

The employer shall be responsible for providing the vouchers as stipulated in item (1), (3) and (4) above.

In addition, some local courts provide more specific criteria for determining whether there is an employment relationship between two parties. For example, the opinions issued by Shanghai High People's Court in 2002 emphasize that a person shall not be deemed as an employee if he/she is not subject to the management, constraint or control by the employer, takes the business risks with his/her own skills, facilities and knowledge, basically does not need to follow the work instructions of the employer and have no subordinate relationships with the employer. Such kind of person could be deemed as an independent contractor.

b. General Differences in Tax Treatment

According to the tax laws of China, employees shall pay individual income tax on the wage and salaries they receive from employers. The tax exemption amount is RMB 3,500 for Chinese employees and RMB 4,800 for foreigners, and then the progressive tax rate in excess of the said specific amount varying from 3% to 45% will apply. Employers should be responsible for withholding employees' individual income tax from the wages and salaries, and then pay it to the tax authority for and on behalf of employees.

The tax treatment under other civil relationships is quite different from that stated above and depends on the specific situations. For example, if an independent contractor provides services to a company and receives remuneration for such personal services, the individual income tax on the remuneration would be paid at the rate of 20% of the balance after deduction of RMB 800 from each income not more than RMB 4,000 or the balance after deduction of 20% of the expenses of each income of more than RMB 4,000.

c. Differences in Benefit Entitlement

Under an employment relationship, employers shall contribute to employees' social insurances (including pension insurance, medical insurance, work-related insurance, maternity insurance and unemployment insurance) and housing reserve fund in accordance with national laws and local regulations. Employees are also entitled to various statutory leaves including but not limited to paid annual leave, marriage leave, maternity leave, paternity leave, work-related injury leave and sick leave. Employers may grant more, but never less than the mandatory minimum level as provided by law. However, on the other hand, independent contractors are, in general, not granted the mandatory social insurances and housing reserve fund, or mandatory paid leaves described above.

d. Differences in Protection from Termination

PRC labor laws generally favor employees and therefore contain many statutory provisions on termination of employees. An employer is only permitted to immediately and unilaterally terminate an employee without severance pay in one of the following circumstances:

- the employee fails to satisfy the employment conditions during the probationary period;
- the employee seriously violates the labor disciplines or the employer's rules and regulations;
- the employee has established an additional employment relationship with another employer, which materially affects the completion of his/her tasks with the employer, or the employee refuses to rectify the matter per the employer's request;

- the employment contract is invalid because the employee used means such as deception or coercion, or took advantage of the employer's difficulties to cause the employer to conclude the contract or to make an amendment thereto, which is contrary to the employer's true intent; or
- the employee is criminally prosecuted under the law.

Furthermore, the employer may terminate an employment contract under any of the following circumstances, but it must give the employee 30 days' prior written notice or one month's salary in lieu of notice, and also must pay severance in accordance with law:

- the employee, after undergoing a legally prescribed period of medical treatment and recuperation for an illness or non-work-related injury, remains unable to perform his/her original job duties, and is also unfit for another job assigned by the employer;
- the employee is incompetent in fulfilling his/her duties, and remains so after undergoing further training or an adjustment of his/her position;
- the employment contract cannot be performed due to any major changes of the objective circumstances under which the contract was originally concluded, and the employer and the employee fail to reach agreement on modification of the contract after mutual consultation.

If the employer intends to initiate a collective redundancy with at least 20 employees or 10% of the total staff being affected, it must satisfy certain conditions and complete the required procedures such as communicating with the trade union or all staff, seeking opinions from the trade union or employee representatives, and filing the redundancy report with the local labor administrative department.

Practitioners and courts in China interpret these statutory termination provisions as exhaustive. In other words, employers cannot add any additional conditions for early termination in its employment contract and use such additional conditions to unilaterally terminate their employees. The only way in which the termination provisions of an employment contract may differ from statutory termination conditions is by optional reference to an employee handbook (also known as a staff handbook) or other internal policies.

Employees may initiate labor arbitrations in response to any unilateral termination by their employers. Either employee or employer may appeal a labor arbitration's decision to the court when feeling dissatisfied with its decision. During the labor arbitration or litigation, the employer must provide solid evidence to support the termination and assume the burden of proof. If the unilateral termination by the employer is finally judged as illegal, the employer must either reinstate the employment with the employee and provide back pay, or pay double statutory severance as compensation for the wrongful termination.

However, termination of an independent contractor is much easier and more flexible. The company may terminate an independent contractor by serving a notification according to the conditions stipulated in the contract for service, or the Contract Law of the People's Republic of China, but does not need to pay severance unless otherwise agreed by the parties. The company and the independent contractor may also agree on a termination at will without cause. Independent contractors are not protected by the provisions of the Labor Contract Law, but if they suffer losses from the company's termination which breaches the contract or law, they may claim compensation for damages.

e. Local Limitations on Use of Independent Contractors

There are no specific limitations on the use of independent contractors in China.

However, employers are not allowed to use nominal independent contractors to avoid their employer liabilities under PRC labor laws. Such relationship with the “nominal independent contractors who are de facto employees” will be penetrated by labor arbitration commissions and courts, and identified as an employment relationship according to the factors as stated above.

f. Other Ramifications of Classification

There are also other ramifications of difference between employees and independent contractors. For instance, employees shall work under one of the three working hours systems (i.e. standard working hours system, flexible working hours system and comprehensive working hours system) based on the nature of their work and positions. However, there are no specific working hour requirements for independent contractors.

In addition, the employer shall bear liability if any third party suffers loss or injury due to the employee's performance of duties. However, based on different types of contractual relations, independent contractors' liabilities for tort may be different. For example, according to Article 10 of Interpretation of the Supreme People's Court on Several Issues Concerning the Application of Law in Hearing Cases of Compensation for Personal Injury, where a contractor causes an injury to a third person when completing certain work, the contractor itself shall bear the liability unless the hirer has any negligence in respect of its order, or instruction or selection of contractors.

g. Leased or Seconded Employees

Under PRC labor laws, it is possible to lease employees to another employer, which could be called “labor dispatch”. Labor dispatch means the labor dispatch agency enters into a labor service contract with an accepting company and then dispatches its employees to the accepting company in exchange of service fees. The dispatched employees work under the instruction and management of the accepting company, but the labor dispatch agency is the legal employer of these employees and shall bear employer liabilities. The main advantage of labor dispatch is flexibility: dispatched employees are not considered regular employees of the accepting company. As a result, many companies used labor dispatch as their main or only method for hiring employees based on the belief that hiring through dispatch agencies could mitigate or avoid employer liability. Against this backdrop, the Labor Contract Law, which came into effect on January 1, 2008, attempted to address this practice by mandating equal rights for employees hired through labor dispatch agencies and “generally” restricting the use of labor dispatch only for “temporary, auxiliary and substitute” jobs. However, labor dispatch agencies have seized on the term “generally” in the law and the vagueness of the terms “temporary, auxiliary and substitute” to argue that there is no real restriction on the use of labor dispatch; as a result, the use of labor dispatch by companies increased rather than decreased. This is contrary to the legislative intent of the law.

In this situation, the Standing Committee promulgated the Decision on Revising the “*Labor Contract Law of the People's Republic of China*” (the “Amendment”) on December 28, 2012, which came into effect on July 1, 2013. The Amendment focuses on labor dispatch issues by addressing the standards for labor dispatch agencies, discussing the general rule of equal pay for equal work, defining the scope of labor dispatch and setting forth the consequences for violating these regulations. To implement this Amendment, the Ministry of Human Resources and Social Security promulgated the *Interim Provisions on Labor Dispatch* (the “Interim Provisions”) on January 24, 2014, which became effective on March 1, 2014. The Interim Provisions describe the criteria for temporary, substitute and auxiliary positions, state the maximum proportion of dispatched employees an accepting company may have, establish the conditions for returning dispatched employees, and contain provisions on social insurance and work-related injury obligations. The

Amendment and the Interim Provisions set strict limitations on labor dispatch, which has caused many companies to transfer dispatched employees to direct hire of employees or use labor outsourcing services as a substitute for labor dispatch to ensure full compliance with law.

On the other hand, there are no specific regulations on secondment of employees. In practice, secondment is used mainly by government agencies and public institutions to complete certain temporary work. Now some private companies may also second employees to other companies, mainly to their affiliated companies or business partners, with their employment relationships with the seconded persons remaining unchanged. Secondment and labor dispatch are very similar. The major difference is that secondment is not for the purpose of profit, and the seconding company shall not receive any remuneration from the accepting company except the reimbursement for the cost in relation to the employees' salaries, social security contributions and other fees payable to the employees during the secondment period.

h. Regulations of the Different Categories of Contracts

In China, employment relationships are bound by various labor and social security laws, including but not limited to, Labor Law, Labor Contract Law, Social Insurance Law and Trade Union Law. The rights and obligations of employees and employers under these laws are quite different from those under general civil legal relationships. The contract for service with an independent contractor is subject to the Civil Law and the Contract Law, observing the principle of autonomy of will, and is more flexible in the conclusion and termination of contracts.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As described above, there are no specific regulations distinguishing “independent contractors” from “employees”. Instead, re-characterization of independent contractors as employees depends on several criteria which have been formulated in the national regulations and developed by local courts for confirmation of employment relationships. The principle is, if a person is deemed to have established an employment relationship with the employer, he/she would be protected by labor laws as an employee; otherwise if he/she is deemed to only have a service relationship with the company, he/she will not be under the protection of labor laws.

b. The Legal Consequences of a Re-Characterisation

If an independent contractor is re-characterized as an employee, he/she would be under the protection of labor laws, and the hirer shall bear employer liabilities and obligations including but not limited to the following:

- entering into a written employment contract with the employee;
- providing the employee with salary no less than the minimum wage standard, granting the employee's right to have breaks and holidays, and observing the regulations on working hours;
- providing the employee with labor conditions and protections as required by labor laws;
- making social insurance and housing reserve fund contributions for the employee;
- providing the employee with benefits no less than the minimum mandatory level, such as paid annual leave, marriage leave, maternity leave, paternity leave, work-related injury leave and sick leave;

- observing the statutory conditions for termination of the employment contract with the employee; and
- providing the employee with severance payment no less than the mandatory level in accordance with law for the termination of the employee;

In particular, if an independent contractor is re-characterized as an employee, and suffers from work-related injury and is identified as having disability while the employer does not contribute to his/her work-related injury insurance, the employer shall be liable for the work-related injury, and bear the cost in accordance with the items and standards of work-related injury insurance benefits, such as the medical cost, life care fees, a lump-sum disability assistance allowance, and a lump-sum medical treatment allowance that should have been covered by the work-related injury insurance.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

In practice, “nominal independent contractors” usually seek the legal status of employees in order to get special protection for employees, such as for the identification of work-related injuries and obtaining relevant compensation, contribution for social insurances and housing reserve fund, and protection from termination. They may file labor arbitration for confirmation of an employment relationship with the employer. When there are sufficient elements that are compatible with the chosen qualification of the employment contract, the contract for service will be re-characterized as an employment contract and the individual concerned will be deemed as an employee. If the labor arbitration fails, the person may bring a lawsuit to the court and then may appeal when dissatisfying with the first-instance judgment.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In the event of re-characterization, upon the employee’s report to the labor administrative department, the employer would be possibly ordered to pay the employee salary no less than the minimum wage standard, and also pay overtime payment when applicable. The employer would also possibly need to pay double wage to the employee for not entering into a written employment contract with the employee.

In addition, the employer would be liable for the unpaid social insurance funds as well as late payment interests. If the employer fails to make a payment of the employee’s social insurance within the period specified by the local labor administrative department, it would be subject to a fine of 1 to 3 times the amount in arrears. Especially, if the employee suffers from a work-related injury, the employer would be liable for the benefits and expenses under a work-related injury insurance.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

It is recommended to draft a written agreement to specify the rights and obligations of the independent contractor and the business. The relationship between the two parties should be structured in a way to avoid elements specific to a subordinate relationship.

The business should keep the following in mind when drafting such an agreement:

- do not stipulate the independent contractor's department, job title, report line, working hour, working place, monthly salary, paid annual leave, social securities, and etc. That are typically contained in an employment contract.

- the employee seriously violates the labor disciplines or the employer's rules and regulations;
- do not stipulate that the independent contractor should work per the superior's instructions or observe the labor disciplines and internal policies of the business;
- it should be stipulated what specific service or work product is required by the business, and when the service or work products should be delivered to the business;
- it should be stipulated that the independent contractor is free to organize his/her work, working time working manner, etc. As long as he/she could provide the service or work product by the deadline as required by the business;
- it should be stipulated that the independent contractor's service fees depends on the quantity and quality of the service or work product completed, and that the business has the right to appraise the service or work product and require the independent contractor to make correction or improvement if the service or work product does not satisfy its requirements;

b. Day-to-Day Management of the Relationship

The general principle is, if the business wishes to avoid re-characterization of an independent contractor as an employee, the business should give the contractor as much independence as reasonably possible, almost as though that contractor were a separate business entity.

Specifically, both the business and the independent contractor must act in consistence with the relationship described in their written agreement. For example, the service fees should be paid in a way different from the salary paid to employees. This means, the fees should not be fixed, but depend on the quantity and quality of each service or work product provided by the independent contractor. Also, the business shall not have any action or statement in connection with the overtime payment, attendance, application for leaves, performance review, disciplines, and etc. for the independent contractor in its daily management.

V. TRENDS AND SPECIFIC CASES

With the promotion of the national strategy of “Internet+” and the popularity of Internet technology, the sharing economy has become the new norm of China’s macro economy and penetrated into all aspects of life. In this process, a large number of new businesses that operate using APPs have emerged and developed very rapidly, especially in the industry of tailored taxi service and door-to-door service. For instance, “Didi”, a taxi-hailing APP, is now operating its business in more than 400 cities in China, with 300 million users registered. This new business model has greatly changed the traditional market and promotes the development of economy. However, on the other hand, these new businesses also encounter many difficult problems. One is the employment issue between the new businesses and their service staff such as drivers providing taxi hailing services. As the new businesses often do not have employment contracts with the service staff, or make social insurance contributions for them, labor disputes have happened frequently and whether an employment relationship exists is a primary issue in most cases.

In practice, labor arbitrators and judges always consider the three elements provided by the Circular as stated in Paragraph II to determine whether the driver is an employee or an independent contractor. For example, Mr. Liu was a salesman of a sales company. His flexible working hours enabled him to drive between clients frequently. In order to make more money, he registered himself on a taxi-hailing APP as a part-time driver. He realized that he could make more money by being a tailored taxi driver than being a salesman,

so he quit his job at the sales company and requested confirmation of his employment relationship with the taxi-hailing APP company. However, the labor arbitrator held that no employment relationship existed between Mr. Liu and the taxi-hailing APP company, because Mr. Liu only uploaded the photocopies of his driver license and car license to the taxi-hailing APP to become a driver, and was never under the management of the company with his remuneration paid through Wechat. Another case is about Mr. Wang who found a job in a taxi-hailing APP company through a recruitment advertisement. The advertisement said that the remuneration for a driver included base salary, service award, security award, full attendance award, overtime allowance, and parking allowance. In addition, the driver must work six days per week and be on line from 6:30 to 9:00 AM and from 17:30 to 22:00 PM every working day. Then in a wage dispute between Mr. Wang and the APP company, the labor arbitrator held that the relationship between the two parties met the basic characteristics of an employment relationship and therefore supported Mr. Wang's claims for the payment of wage. The cases above reflect the application of the determination rules of employment relationships, however, the Circular was released about ten years ago and the market has greatly changed. The employment mode of the new businesses such as APP Companies is also quite different from that of traditional businesses.

Therefore, it is questionable whether the rules provided by the Circular should be used to determine an employment relationship in the labor disputes between new businesses and the service staff.

In order to better regulate, manage and guide the tailored taxi service in China, the Ministry of Transport and other six ministries issued the Interim Administration Measures for Network Booking of Taxi Business Services (hereinafter referred to as the "Interim Measures") in July 2016. The Interim Measures expressly require taxi-hailing APP Companies to sign employment contracts or other agreements with drivers according to drivers' working hours, service frequency, and etc. This means the taxi-hailing APP Companies are not mandatorily required to establish employment relationships with the drivers, and it would still be a difficult issue to determine whether a driver is an employee or an independent contractor when there is no employment contract.

VI. CONCLUSION

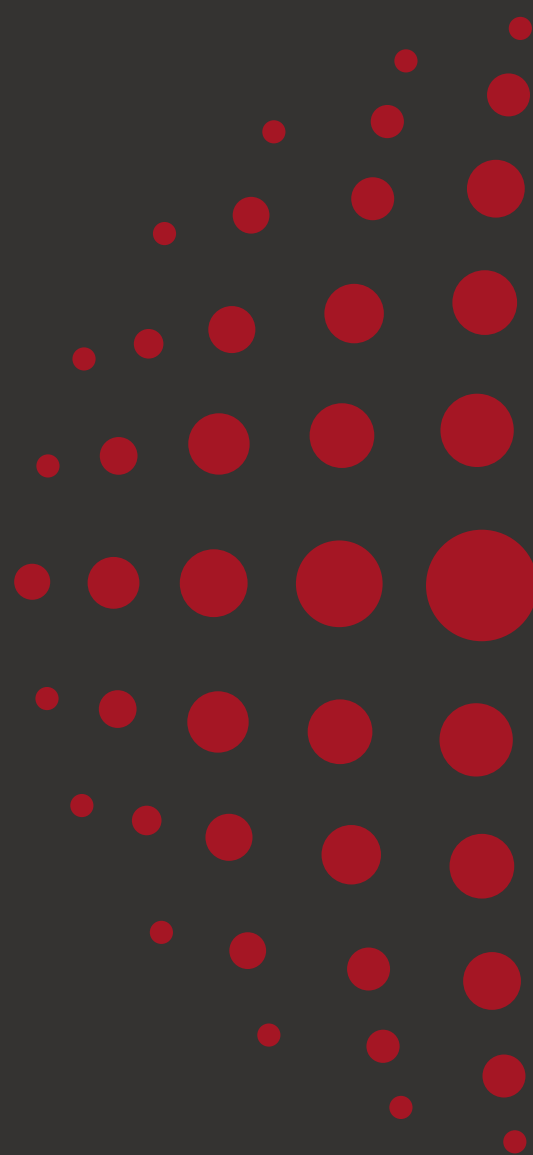
In China, businesses may, based on its autonomy in management and to the extent permitted by law, decide at its own discretion to engage outsiders to do certain work or provide certain services by entering into a civil contract for service with the individuals. However, the relationship between the businesses and the individuals would be easily confused with the employment relationship under the labor laws of China. It is often that such individuals seek the status of employees by filing labor arbitration to request confirmation of the employment relationship.

If they are finally re-characterized as employees, they would be protected by labor laws and regulations, otherwise, they would be probably deemed as independent contractors and their relationships with the businesses would be bound by civil laws.

In practice, it is not easy to distinguish independent contractors from employees. If the business wants to avoid re-characterization of independent contractors as employees, it must structure its written agreement with independent contractors carefully and skillfully to make the items obviously different from the stipulations in a typical employment contract. What's more, in its daily management, the business should not have much management or control of the independent contractors to avoid formation of a subordinate relationship.

Meanwhile, the business shall observe the principle of good faith and shall not willfully evade employer liabilities by entering into false contracts for service with the individuals who are de facto employees. Otherwise, these individuals will likely be re-characterized as employees by labor arbitrators and judges in the event of labor dispute, and the business would be finally required to bear employer liabilities.

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COLOMBIA

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I. OVERVIEW

a. Introduction

Colombian legislation recognizes a difference between the relationships derived from the rendering of services by an individual in an independent manner and those carried out under the subordination of a person or corporate entity, which benefits from the rendered services. The former is recognized as a “services agreement” whereas the latter is recognized as an “employment agreement”. It is necessary to clarify that Colombian labor law does not define or regulate services agreements since these are governed by commercial, civil or public law provisions depending on the nature of the agreement and the parties involved.

Services agreements are characterized by the autonomy and independence of the contractors during the performance of their duties, the time limited nature of the relationship with the contracting company/individual, the absence of a schedule or working day, the possibility of rendering their services outside the contracting party’s facilities and the use of their own working tools. Between the independent contractor and the contracting company/individual there is no labor relationship and independent contractors are not entitled to receive fringe benefits, vacations, nor any other rights derived from an employment agreement.¹

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The main element that distinguishes an employment relationship from a commercial or civil one is subordination, which has been understood by the Colombian Constitutional Court as the *“permanent juridical power by means of which the employer directs the labor activity of the employee, through the issuance of orders and instructions and the imposition of regulations regarding the manner in which the employee must carry its functions and comply with its obligations”*.²

Accordingly, subordination is the distinctive element of employment relationships. In contrast, the lack of it derives from the autonomy of the person who is rendering his/her services. Thus, under services contracts:

- the contractor assumes all risks and operates with its own resources; and
- the contractor acts with full economic, technical and administrative autonomy.

This distinction is applicable regardless of what the parties may have agreed in writing. Colombian labor legislation is governed by the primacy of reality principle (meaning one has to look at the reality of the relationship), according to which an employment agreement is deemed to exist in those situations whereby an individual undertakes to render a personal service to another individual or a corporate entity, under a relationship of continuous dependence or subordination to the individual or corporate entity, receiving remuneration as consideration.

Therefore, an employment agreement is deemed to exist when the three above mentioned factors, specifically the rendering of a personal service, continued dependence or subordination, and remuneration exist concurrently. An employment agreement does not cease to exist simply because of the name given to it, or any other conditions or

¹ Ministry of Labor. “Legal Concept.” ID 168781. Bogota D.C., September 30, 2014 and Colombian Supreme Court of Justice, Decision 37995 of October 26 of 2010.

² Colombian Constitutional Court, Decision C-386 of 2000

modalities that may be added to it.

Colombian laws and case law clearly state that no matter what the parties agree upon in writing, what is really important is the manner in which the services are actually rendered.

Accordingly, and from the labor perspective, an individual who agrees with another person or with a legal entity to execute some specific tasks without being subordinated to the contacting party will be considered to be an independent contractor. In this regards, the following are the inherent characteristics of a service agreement to be rendered by an individual:

- the contracted tasks have a determined price;
- the contractor assumes the inherent risks involved in the execution of the contracted services;
- the contractor makes use of his/her own resources both (technical, economic, financial and/or human), for the performance of the contracted activities; and
- the contractor has full technical and administrative autonomy in order to manage his/her staff.

b. General Differences in Tax Treatment

Usually, for tax purposes, individuals in Colombia are classified in one of two tax categories, namely residents or non-residents.

An individual is considered to be a tax resident when they have spent over 183 days in Colombia in a 365 day period. In addition to this, individuals with Colombian citizenship are considered to be tax residents if certain criteria are met (i.e. amount of income sourced in Colombia or assets held in Colombia, the individual's country of residence, family's country of residence, etc.).

These categories are important because Colombian tax residents are subject to income tax on their worldwide income and equity, while non-residents are only subject to income tax over their Colombian source income.

Given the recent tax reform (Law 1819 of December 29, 2016), the income obtained by a Colombian tax resident will be taxed on a different basis and rates, depending on the schedule in which such income is classified.

In this sense, the labor schedule is applicable to the income derived from: (i) a labor contract; or (ii) the income obtained working as an independent contractor, provided he/she does not hire two or more individuals associated with the service rendered for a period of at least 90 days. Such income would be subject to taxation at progressive marginal rates of 0%, 19%, 28% and 33%, depending on the amount of such income received by the individual. Some legal deductions in this schedule are allowed, but they cannot exceed 40% of the taxable income, without exceeding in any case a total of 5.040 UVT (approx. COP159.208.560 / USD53.070).

There is also a non-labor income schedule that is applicable, among others, to the income obtained by those independent contractors who hire two or more individuals associated with the service rendered for a period of at least 90 days. Such income would be subject to taxation at progressive marginal rates of 0%, 10%, 20%, 30%, 33% and 35%, depending on the amount of such income received by the individual. Again, some legal deductions in this schedule can also be made, but these deductions cannot exceed 10% of the net taxable income, without exceeding in any case a total of 1.000 UVT (approx. COP31.589.000 / USD10.530).

The rate of 'withholding tax' applicable to payments made by an employer to an individual will vary depending on the amount of income obtained by the individual during the respective month. In this sense, progressive marginal rates of 0%, 19%, 28% and 33% are applicable to the gross payments, minus allowed deductions (i.e. mandatory health and pension contributions, voluntary contributions to private pension funds, 25% of the net income which is considered exempt, etc.). These withholding tax rates are also applicable to those individuals who earn their income as independent contractors who do not hire two or more individuals associated with the service rendered.

In the event that a person earns his / her income as an independent contractor and does hire two or more individuals associated with the service rendered, such income would be subject to an 11% withholding tax if the contractor is obliged to file an income tax return. Otherwise, a 10% withholding tax is applicable.

All Colombian employers are responsible for the payment of payroll taxes, which are contributions that every employer has to make for each one of its employees who earn more than 10 minimal monthly legal wages (approx. COP 7.377.170/ USD2.460). Such payments have to be made on the basis of the salary at a 3% rate destined to the Colombian Family Welfare Institute (*Instituto Colombiano de Bienestar Familiar - "ICBF"*), 2% destined to the National Apprenticeship Service (*Servicio Nacional de Aprendizaje - "SENA"*) and a 4% destined to the Family Compensation Funds (*Cajas de Compensación Familiar*). The payroll taxes only have to be paid for the individuals that work under a labor contract. The payroll taxes do not have to be paid for those individuals working as independent contractors.

Non-residents

As previously mentioned, non-residents are only subject to Colombian income tax over their Colombian source income.

Non-residents are not obliged to file an income tax return if all of their Colombian source income was subject to withholding tax. Generally, all payments made by Colombian employers or companies to non-resident individuals are subject to withholding tax.

In light of the recent tax reform, the withholding tax rate for non-residents is 15% of their gross income. Therefore, the payments made to non-resident individuals for personal services rendered through a labor contract or as an independent contractor, would be subject to a 15% withholding tax over the gross payment, which will be the final tax due in Colombia, since such individuals would not be obliged to file an income tax return.

c. Differences in Benefit Entitlement

Employment relationships are governed by the Colombian Labor Code, which establishes several legal benefits to employees depending on the amount of their salary and the fact that such salary is ordinary or all-inclusive. Employees earning more the thirteen monthly minimum wages ("*SMLMV*") can agree with their employer to have an all-inclusive salary which means that they will not be entitled to fringe benefits. For 2017, the SMLMV was fixed on COP 737,717.

On the other hand, since the Colombian Labor Code is not applicable to commercial or civil relationships such as those governed by services agreements, independent contractors do not have the benefits or the rights to which employees are entitled. They will only have the payments and benefits agreed upon in their services agreement.

Colombian labor law establishes the following benefits for employees under an employment agreement:

Transportation Aid: This is a monthly aid provided by the employer to employees who earn less than 2 SMLMV (COP 1,475,434 for 2017) and who have to commute by their own means. The monthly amount of the transportation aid is established annually by the National Government (COP 83,140 for 2017);

Dress and Footwear: Three times a year, the employer must provide one pair of shoes and one set of work wear clothes to employees who earn less than 2 SMLMV;

Severance Payment (“Cesantías”): Employees who receive an ordinary salary are entitled to a severance payment, which is one month's salary per year, or proportional to the time worked. The severance payment must be deposited in the severance fund chosen by the employee. Severance payments can only be withdrawn or paid directly to the employee at the termination of the employment or in some specific cases related to housing or studies;

Interest on Severance: Employees who receive an ordinary salary are entitled to interest on their severance payment, equivalent to an annual rate of 12% of the severance, or a proportion if the employee worked for less than 12 months during the year. This payment is received directly by the employee at the end of each calendar year or on termination of employment;

Premium Services: A monthly salary paid in 2 installments, being 15 days of salary on the last day of June, and the remaining 15 days of salary during the first twenty days of December; and

Vacations: 15 days of paid rest for each year of service, which can also be paid pro rata to the time during which the employee worked.

These benefits are granted by virtue of the law and apply in every labor relationship. However an employer may also decide to grant additional benefits to employees, such as bonuses, food vouchers, and other kinds of benefits, which may be given or removed, depending on any agreements made between the parties, or in a non-unionized collective agreement (“*pacto colectivo*”).

Additionally, if the employees are unionized, they will also have the benefits and prerogatives established within the corresponding collective bargaining agreement.

In contrast, independent contractors are not entitled to receive legal benefits established by labor law. Independent contractors are entitled to the fees agreed between the parties which are not even limited to a minimum wage. In this sense, it is important to highlight the fact that the work relationship between the contracting party and the contractor is of a civil or commercial nature, and the benefits the contractor is entitled to will depend on the specific agreement between the parties and not on any labor regulation.

d. Differences in Protection from Termination

Employees

With the exception of labor stability rights (security of employment) cases and collective dismissals, any employment agreement may be unilaterally terminated by the employer without cause (redundancy) by paying a legal indemnification depending on the:

- time for services for indefinite term contracts;
- time remaining for the occurrence of the established date;
- termination of the completion of the hired task in cases of fixed term employment agreements; or
- the duration of a specific task.

As per the stability rights and prohibition of collective dismissals, protection from termination for employees depends on the condition or employment status of the individual and/or the type of agreement. As mentioned earlier, any employment agreement can be terminated unilaterally by an employee, by paying them a legal indemnification, however there are some restrictions related to:

- the health condition of the employee;
- the fact that the employee is part of a union and his/her position within the union;
- workplace harassment cases; and
- the number of employees¹ contracts that can be terminated by redundancy.

With the exception of the termination of the contracts of unionized employees (which can also be terminated with the authorization of a labor judge), prior authorization from the Ministry of Labor is required for unilateral termination of the contracts of employees with stability (or security of employment) rights derived from their health limitations, pregnancy or because they have made a complaint of workplace harassment. In these cases, the employer must argue that the cause for termination was fair and request approval from the labor inspector. Without such authorization, the termination will not be valid and the employee may claim reinstatement before a labor judge and/or a constitutional judge.

In union matters, the union's board of directors and the members of the commission of claims will have permanent stability rights during their employment; the founders of the union will have the same right for six months from the incorporation of the union. In the event of a collective dispute, the employees involved cannot be terminated without cause; however authorization from the Ministry of Labor is not required.

In addition, Colombian labor laws establish a limit to the number of employment contracts that can be terminated due to redundancy, and as a result of this a company cannot dismiss, without cause, more than a certain number of employees within a period of six months without prior authorization from the Ministry of Labor. These limits depend on the number of employees employed by the company, and failure to comply with the limits will result in the declaration of the existence of a collective dismissal.

If the Ministry of Labor decides that a collective dismissal exists, all employees terminated without cause during the restricted period must be reinstated.

In any of the reinstatement scenarios mentioned above, the employer must pay salaries, fringe benefits, social security contributions and payroll taxes as of the date of termination until the effective date of reinstatement.

Independent contractors

Protection from termination for independent contractors is limited to what may have been agreed upon in their services agreements. However, if an independent contractor is terminated and he/she manages to prove before a labor or constitutional judge that he/she was rendering services under a *de facto* employment relationship, the re-characterized employee will have the protection granted to employees pursuant to the Colombian labor laws mentioned in section II d i.

As previously mentioned, independent contractors are not governed by labor regulations, but by civil, commercial or public laws. In this sense, they are not entitled to labor legal compensations or stability rights at termination, except in the case of extreme necessity derived from health complications.

If the independent contractor is in a situation of extreme necessity because of his/her health complications, the contracting party shall not terminate or refuse to renew the

contract based on the health condition of the contractor. In this case, the contractor may file a constitutional action where the constitutional judge will have to determine if (a) the contractor's integrity (or employment status) is at risk because of the termination, and (b) the termination or non-renewal was based on a discriminatory act from the contracting party in consideration of the contractor's health condition.³

If it was expressly agreed in the service agreement that some type of compensation or economic penalty for failure to comply with the obligations will be payable, the party who fails to comply with their obligations will need to pay the agreed compensation.

On the other hand, there is a specific kind of services agreement, being the commercial agency agreement, which will be set out in section *II f* (Other Ramifications of Classification). In the event of termination of the commercial agency agreement, for any cause, the commercial agent is entitled to a commercial severance equivalent to one twelfth of the average commission, royalty or profit earned by the agent during the last three years, multiplied by the number of years of duration of the agreement, or to the average of all sums received if the duration of the agreement is shorter.

Moreover, if the commercial agency agreement is terminated without cause, the commercial agent would be entitled to an equitable indemnification which shall be assessed in court where the agent will have to evidence the damages suffered upon termination.

e. Local Limitations on Use of Independent Contractors

According to the current regulations, it is possible for an individual or legal entity to arrange for one or several activities to be carried out by means of a services agreement. The essential characteristics of an independent contractor are:

- they are an individual or legal entity;
- they carry out one or several activities or the provision of services for the benefit of third parties;
- that the work or services require the payment of a set or determinable price;
- that the contractor assumes all the risks and operates with his own means; and
- that the contractor acts with full technical, financial, administrative and managerial autonomy. Given that the independent contractors will provide their services in an independent and proper manner without risk of re-characterization, there is one recent limitation to the use of independent contractors established by Decree 583 of 2016.

Pursuant to this Decree, companies are not allowed to outsource the provision of services related to their core business activities whenever the constitutional and legal rights of the outsourced employees are affected.

Core business activities could be defined as those related to the production of goods or the rendering of services characteristic of the company that are essential for the development of its business because without them the operation of the company would be affected.

In addition, it would be necessary that the outsourcing company does not comply with its legal and constitutional obligations towards its own employees in order for the outsourcing to be deemed illegal.

As a consequence, companies and public entities are not allowed to hire personnel for

³ This position has been adopted by the Colombian Constitutional Court in recent decisions such as; (i) Decision T-988 of 2012, and (ii) Decision T-040 of 2016

the development of their core business activities through any form of intermediation, such as independent contractors or co-operatives of associated work. Yet, in Colombia the provision of personnel through temporary services companies is allowed, but only in the cases authorized by law.

f. Other Ramifications of Classification

Associated Labor Cooperatives

In addition to independent contractors and temporary employees, there is a third category of co-operated employee which belongs to Associated Labor Cooperatives, which are non-profit organizations which bring together people who participate in management and make economic contributions, including their own work, to the cooperative. The aim of cooperatives is to produce goods, carry out works or provide services in common, through processes or sub-processes. Likewise, cooperatives have ownership of all the means of production and/or labor, such as the facilities, equipment, machines and technology. Associated work is ruled by its own statutes, and thus the regulation laid down by the Colombian Labor Code does not apply to them.

Associated Labor Co-operatives are explicitly prohibited from acting as labor intermediaries or to provide workers, under penalty of sanctions, which may be of up to 5000 SMLMV (COP 3,688,585,000 for 2017) both for the co-operative and the beneficiary of the services.

Commercial Agencies

According to the Colombian Commerce Code, a commercial agency agreement is a contract under which an agent shall promote and exploit (in an independent and stable way) the business of the principal within a specific territory in Colombia, acting as a representative or agent of a national or foreign entrepreneur.

In accordance with Colombian case law and legal doctrine, the main elements of a commercial agency contract are that the:

- agent must be independent;
- relationship between the agent and the principal must be stable;
- agent must have engaged to promote or exploit the business of the principal;
- agent must act for the account and benefit of the principal; and
- agent must receive a monetary compensation for its services.

Whenever the elements of the commercial agency agreement are present in the execution of a commercial relationship, a *de facto* agency will be deemed to exist, and therefore, the commercial agency provisions incorporated in the Colombian Commerce Code shall apply regardless of the existence or not of a written agreement between the agent and the entrepreneur.

Upon termination of the agreement, the agent has the right to receive from the principal the following statutory payments:

- commercial severance payment (*cesantia comercial*); and
- equitable indemnification if the termination takes place without cause.

These payments are explained in section *II d ii*.

g. Leased or Seconded Employees

Temporary services companies

Companies in Colombia can only hire the provision of temporary personnel through

temporary services companies in certain circumstances, namely:

- occasional, accidental or transitory tasks, as those described in Article 6 of the Colombian Labor Code;
- replacing personnel on vacations, licenses or medical leaves; and
- to respond to increases in production, transportation, sales of products and merchandises, crop periods and the rendering of services for a term of six (6) months renewable for another six (6) months.

It is important to highlight that according to labor solidarity, as set out in Colombian labor laws, means that unless a temporary services company has complied with social security contributions in a timely manner, the beneficiary of the services (the company) can be held jointly and severally liable with the temporary services company for the salaries, social security contributions and/or social benefits to which employees are entitled to.

Labor laws state that if the legal term provided for hiring temporary personnel is exceeded, the temporary services company will be deemed as a simple intermediary and the beneficiary company will be deemed to be the real employer of those temporary employees who exceed the legal term. Therefore, if the legal term is exceeded, the beneficiary company will be liable for all labor payments due and could be subject to fines from the Ministry of Labor of up to 100 SMLMV (COP 73,771,700 for 2017) during the time the transgression continues, plus a sole fine of up to 5000 SMLM (COP 3,688,585,000 for 2017) for the violation of general labor laws.

Outsourcing

Pursuant to Colombian labor laws, companies are allowed to outsource different kinds of services or processes through a third party provider, as long as such activities are not part of the core business of the contracting party.

In these cases the outsourcing company will autonomously perform all technical and administrative activities for which it was hired. This means that the contracting party is not authorized to give orders to the outsourcing company, nor its employees on the time, mode, place and amount of work.

Only general instructions can be given on how the services should be performed, which is why the conditions for the execution of the contract should be set out in the same document or services agreement, which guarantees the delivery of the service under the guidelines previously defined for the operation.

When this type of engagement is used, the outsourcing company is the sole employer of the employees rendering services for the contracting company, and as such, the outsourcing company will be bound to comply with all applicable legal obligations in Colombia as the employer.

It is important to highlight that Colombian labor law states that, unless the outsourcing company has complied with labor and social security obligations in a complete and timely manner, the contracting company can be held jointly and severally liable with the outsourcing company for all labor and social security payments employees are entitled to.

In the event that the employees of the outsourcing company develop the contracted services without acting independently and instead follow direct orders from the contracting company, it is very possible that the three elements of a working relationship (salary, personal activity and subordination), will be present forcing the companies to comply with all obligations arising from them, in addition to claims brought by employees.

h. Regulations of the Different Categories of Contracts

All employment relationships are governed by the Colombian Labor Code and its complementary laws and decrees. Such regulations are mandatory, meaning that parties to an employment agreement cannot agree conditions less favorable for employee than those set out in law.

As a consequence of this, employees are not allowed to give away their minimum rights granted by the constitution and the Colombian labor laws. In addition, employment conditions such as salary, cannot be unilaterally modified by an employer in a disadvantageous way to the employee.

As per the different categories of contracts, the Colombian labor legislation provides for four types of employment agreements, dependent on their agreed duration:

Indefinite term employment agreement: The duration of this type of agreement is indefinite and is not determined by the parties or by the nature of the work for which the employee is hired. Unless there is an express provision otherwise, employment agreements are understood to be open-ended.

Fixed term employment agreement: These agreements must be set out in writing and can be for a term of up to three years, renewable indefinitely. In the case of fixed-term agreements for less than a year, the parties can agree to renew it successively but after the third renewal, the term of the agreement cannot be less than one year, and any subsequent renewal must be made for at least one year. In order to terminate this type of employment agreement on grounds of contract expiration, the employer must notify the employee of its intention not to renew the contract, at least 30 days prior to the expiration date of the agreement or its current extension. In the absence of such notice, the agreement will automatically be renewed for a period equal to the initially agreed duration.

Agreement for the Duration of the Work: In this type of agreement, the duration is determined by the time required to perform the work that the employee was hired to do. The agreement must be written and the work or activity must be clearly detailed in order to determine when the agreement is due to expire. This type of contract cannot be renewed.

Occasional, accidental or temporary contract: This type of contract cannot exceed one calendar month in duration and is characterized by satisfying the extraordinary needs of the company. The purpose of this type of contract is for the temporary or special needs of the employer, as opposed to the core business activity of the employer.

Civil, commercial and public law regulates services agreements with individuals and companies. Each branch of law sets out special powers and regulations depending on the needs and nature of the service.

From a tax law perspective, independent contractors are classified as:

- independent workers self-employed individuals who are not bound by a contract and their remuneration consists of fees, commissions or servoces.
- independent contractors bound by a services agreement, and their remuneration consists of fees and/or commissions.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

According to the Colombian labor legislation, by virtue of the primacy of the 'reality principle', every agreement under which an individual obliges himself/herself to provide to another person a personal service under continuous dependence or subordination and receives remuneration for the work performed, is considered to be an employment relationship.

Therefore, the employment agreement subject to the Colombian labor regime is deemed when the three above mentioned items (rendering of personal service, continued dependence or subordination, and remuneration) occur, and an employment agreement does not cease to exist simply because of the name given to the agreement entered into by the parties or any other conditions that may be added to it.

Colombian legislation is governed by the territoriality principle, whereby it is assumed that the Colombian Labor Code is applicable to foreigners and nationals, whenever they render their services within Colombian territory.

b. The Legal Consequences of a Re-Characterisation

Re-characterization can only be declared by a labor or constitutional judge, by request of the individual who rendered the services or his/her successors. The legal consequences of a re-characterization are that the former contractor, now employee, will be entitled to all rights and prerogatives derived from an employment relationship. Though, it must be pointed out that except for some specific cases, the rights derived from the existence of an employment relationship will have a statute of limitations of three years from the date when the employee was entitled to such rights. In the case of severance payment, the statutes of limitations will begin to run as from the date of termination of the employment.

Thus, if a contractor succeeds in his/her re-characterization claims, he/she will be entitled to all benefits granted to employees, depending on the compensation that he/used to receive under his/her former services agreement. Among these benefits there are the vacations, legal bonus, severance payment and interest thereon, transportation aid and dress and footwear. In addition, the employer will have to make the corresponding contributions to social security and payroll taxes considering that the individual who rendered his / her services was an employee; payroll taxes have a statute of limitations of five years. Finally rights and obligations necessary for obtaining a pension do not have statutes of limitations.

Labor costs can amount to approximately 55% of monthly fees earned.

Moreover, in the event of an accident and/or illness and/or health condition during the performance of his / her services in Colombia, the individual and/or his / her successors may claim the payment of the assistance and economic benefits not covered by the Colombian Social Security Regime. Such benefits may vary from:

- medical expenses and/or treatments;
- medical leave payments;
- disability indemnifications;
- disability pension;
- survivors pension; and
- allowances for death expenses.

Furthermore, an individual may claim at any time in the future, payment of the pension contributions that should have been made during the time of rendering of services in Colombia, since there is no statute of limitations when dealing with pension contributions.

It must be considered that re-characterization can be done after termination of the *de facto* employment relationship. In this case, the dismissed employee would not only be entitled to the indemnification payments prescribed by law depending on the type of employment agreement, but he/she will also be protected by the stability (protection of employment) rights granted to pregnant employees or those with health complications. Thus, if the re-characterized employee had stability rights at the time of termination, then he/she will be entitled to reinstatement and payment of any salary due, fringe benefits and social security contributions as from the date of the dismissal until the effective reinstatement.

Moreover, when a temporary services agreement is terminated, the contracting party does not pay fringe benefits to the terminated contractor so a re-characterization of such into an employment agreement will mean that employer does not pay fringe benefits at termination.

If the constitutional or labor judge determines that fringe benefits were not paid by the re-characterized employer in bad faith, it will order the employer to pay a legal indemnification consisting of one day of salary for each day of delay as of the termination of the employment agreement. Though, it will not be necessary to prove bad faith regarding non-compliance or delays in severance payments, in this case, the indemnification of one day of salary per day of delay will be counted yearly.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The individual may file a complaint before the ordinary labor jurisdiction or a constitutional action before any judge whenever his/her fundamental rights are being transgressed.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The potential risk arising from non-compliance with contributions to the health system and payroll taxes for an employee on the mandatory percentages, is that the social security entities (either health promoting entities, pension entities, or payroll entities) may initiate an investigation against the employer which may result in fines corresponding to the payment of very high default interests, plus the sums that were not paid because the company did not consider them to be salary.

Additionally, if the Pension and Payroll Taxes Control Unit ("UGPP") initiates an investigation and finds any inaccuracy in the payments of social security system contributions or payroll taxes, it may impose fines on the employer that will range between 20% to 60% of the difference between the amounts paid and the amounts that should have been paid, plus default interests over amounts owed.

In the same order, the Ministry of Labor can impose a fine on the employer ranging from one Colombian minimum wage up to 5000 SMLMV (COP 3,688,585,000 for 2017).

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

In order to establish a clear difference between an independent contractor and an

employee when documenting the relationship in an agreement, the following must be clearly stated:

- the services to be rendered by the independent contractor must be clearly determined and limited to a precise scope of services;
- the duration of the agreements is limited to a period of time;
- it must be clearly stated that the relationship is civil or commercial and the agreement will not be governed by labor laws;
- the inclusion of legal benefits granted to employees must be avoided;
- the payment cannot be documented as "*salary*" but as "*fees*"; and
- it must be clearly stated that the independent contractor is the owner of his/her own tools and equipment to perform the hired activity.

b. Day-to-Day Management of the Relationship

In order to maintain a civil or commercial work relationship it is important for the contracting party to maintain the independence of the contractors whenever they are rendering their services as well as the independence of the employees of the independent contractors; by not giving the contractors any elements that are normally given to actual employees of the company; by making sure that the contractors comply with social security registers and payments as independent contractors requesting proofs of registrations and monthly payments; and verifying how the personnel of the independent contractor are being engaged, if the independent contractor has subordinated personnel. This should be achieved through an employment agreement.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

A bill granting stability (or security of employment) rights to pregnant independent contractors is currently being discussed in the Congress, and has already passed through the second of four debates to be approved by the Colombian Congress and sanctioned by the president. If approved, pregnant women will be entitled to maternity leave for 18 weeks after the birth and stability rights during the pregnancy and the maternity leave meaning that their services agreement will not be able to be terminated without prior authorization from the Ministry of Labor during this period.

b. Recent Amendments to the Law

The Ministry of Labor issued Decree 1563 of 2016 which establishes the rules of affiliation to the Occupational Risks System for self-employed workers /independent contractors without a civil or commercial contract, or employment relationship and who voluntarily want to join the system to have the coverage, welfare and economic benefits. With this Decree the government seeks to advance the formalization of informal workers, as a strategy to contribute to their well-being and that of their family, within the framework of a preventive culture articulated with public health and safety policies at work.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

The Colombian Tax Code provides a statutory definition of permanent establishment, which mainly includes the OECD Model Tax Convention's definition of Article 5. In

addition to the statutory provision, the tax treaty permanent establishment definition applies when they exist. Colombia has a growing network of Double Taxation Agreements, including treaties concluded with: India, Czech Republic, Korea, Mexico, Chile, Switzerland, Canada, Portugal, France and the United Kingdom (however the last two treaties are not yet in force).

The analysis of whether a permanent establishment may arise in Colombia as a consequence of the engagement of one or more individuals in the country mainly depends on whether the individual hired in Colombia can be considered to be a dependent agent, who habitually exercises an authority to conclude contracts in the name of its foreign contracting party. In this case, a permanent establishment of the foreign employer will arise in Colombia under the terms of the dependent agent rule, even if the foreign employer does not have a fixed place of business in the country.

However, consistent with the OECD Model, the Colombian statutory provision includes some exceptions to the existence of a permanent establishment, namely if the dependent agent has no authority to negotiate substantial elements of an agreement or to legally bind the foreign entity within Colombia. If the employee will not have the legal capacity to bind the foreign entity, this should significantly mitigate the permanent establishment risk from a dependent agent point of view.

Currently there are no judicial precedents, which we know of, declaring the existence of a permanent establishment in Colombia under the dependent agent rule.

VII. CONCLUSION

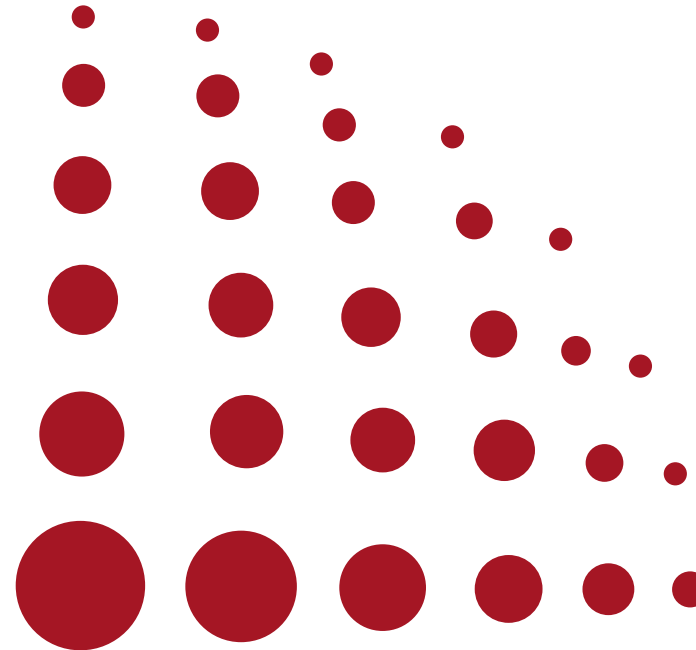
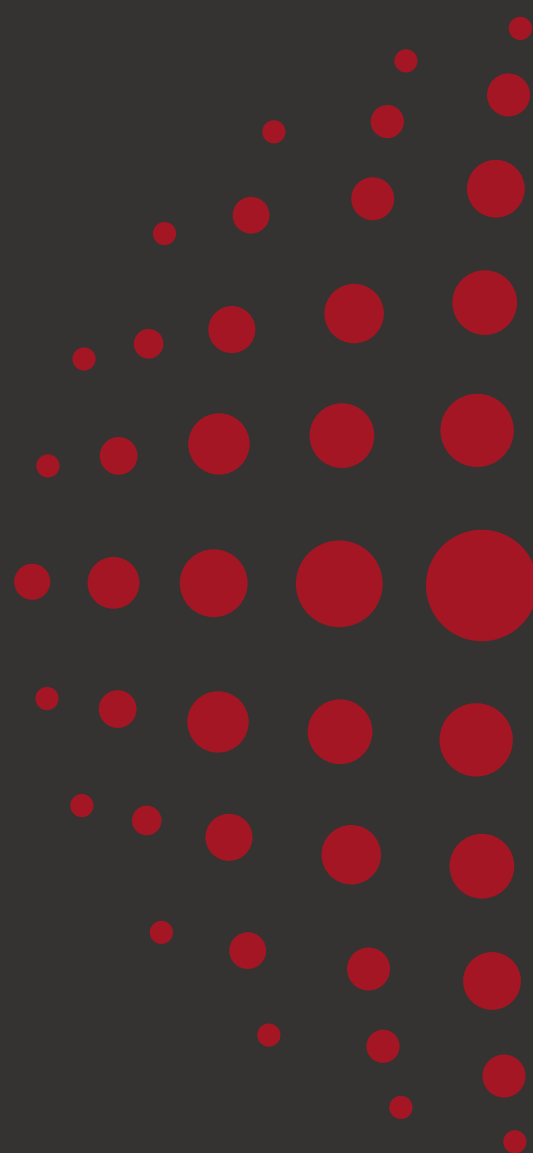
Although labor law deals with legal regulation resulting from an employment agreement, independent contractors cannot be disassociated from the scope of subjects of every day labor law. The employment status of independent contractors means that they are used for the provision of highly technical and specialized services and requires a comprehensive planning strategy for proper decision-making, regarding whether or not it is convenient to contract externally for activities which have been done internally by the company in the past, with a rigorous analysis of the consequence of the loss of control of this activity.

One of the great challenges facing labor law in Colombia is the need to reorganize its instruments of legal and judicial protection, while bearing in mind the social, economic and administrative reality, and in some way to protect legally autonomous labor providers (independent contractors), whose situation is similar to that of a subordinate employee. Leaving independent contractors to exclusively civil/commercial protection may be insufficient, and the law in general must seek to protect the work, regardless of whether it is subordinate or not. Consequently, we applaud the recent developments mentioned above on social security matters for independent contractors. Such developments contribute to the creation of labor equality.

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CZECH REPUBLIC

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I. OVERVIEW

a. Introduction

Czech Republic Labour Market – Key Facts¹

- **Czech Population:** 10,570,000 citizens.
- **current employment rate:** 58,1% (6.141.000 citizens).
- **General unemployment rate:** 3,6% (380.000 citizens).
- **Average Gross wages** (3rd quarter of 2016): CZK 27,220, (EUR 1,010); Average Gross wages in Prague (3rd quarter of 2016): CZK: 34,683, (EUR 1,290).

Currently seven percent of the total working population are self-employed workers/independent contractors in information technology. Freelancing is relatively common practice in the service industry.

As in other jurisdictions, the use of self-employed workers/independent contractors instead of, or as well as employees is not, from a legal point of view, risk free. If an agreement with a self-employed worker is intended to act as a substitute for an employment contract, the agreement will be assessed according to its true nature. Therefore, replacing a contract of employment with any civil law contract, (while meeting the usual criteria of labour employment), actually represents an administrative offence. The employer could be fined between CZK 10,000,000 (EUR 370,000) and CZK 50,000 (EUR 1,900) for such an offence. The employer will also be liable for health insurance and social security contributions for the employee, including a duty of payment of overhead surcharges, related interests and sanctions.

At the same time, it should be acknowledged that the distinction between employees and self-employed workers/independent contractors is a legally difficult task. There are usually only subtle differences between a contract of employment and a civil law contract. It is probably no surprise though that there are substantial differences between self-employed workers/independent contractors within various sectors.

It is usually a relatively simple task to correctly distinguish employees from self-employed workers/independent contractors within large sectors such as; industry, construction, health-care provision etc. However, it is much harder to accurately assess the true nature of “soft” services provided by individuals within sectors such as; information technologies, communication, tourism, various sorts of administrative support and other activities with a predominantly intellectual value added.

Generally speaking, the information technology sector, including areas such as; the internet, modern telecommunication and social networks, has been the one of the first sectors to see an increase in the use of self-employed workers/independent contractors. This may be due to the fact that within these areas, the use of self-employed workers/independent contractors is easier to defend from a legal point of view compared to the use of independent contractors within traditional areas with a predominantly manual and/or strictly organised work.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

In the Czech Republic, the distinction between an employee and a self-employed worker/independent contractor is primarily regulated by the Czech Labour Code. There is a relatively strict assessment under basic characteristics of dependant work as defined in

¹ <https://www.czso.cz/web/czso/404->

the introductory provisions of the Czech Labour Code. This is a preliminary regulation and is interpreted by the courts, namely by the Czech Supreme Court and the Supreme Administrative Court. These courts deal with contentious cases, which often arise as a result of the subtle differences mentioned above. The cases involve either a contract of employment or a civil law contract.

The question of whether an individual is an employee or a self-employed worker/independent contractor by status may be asked in various situations, for example; it may be based on a complaint submitted by an individual to the regional branch of the Labour Office and related control of the Labour Office or to the bodies responsible for the inspection of work, in a dispute about the termination of a contract (or the pseudo-contractor may claim permanent employment with the employer) or during a control being made with respect to the payment of social security contributions etc.

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

In the Czech Republic, the prevailing legal relationship is still the employment law relationship. Pursuant to the Czech Labour Code the employment law relationship includes three different forms:

- the contract of employment – basic and widespread form of the employment law relationship, which provides for work within the full-time weekly working hours up to 40 hours per week;
- the Agreement to Complete a Job - the scope of work for which an agreement to complete a job is concluded may not exceed 300 hours in a calendar year; and
- the Agreement to Perform Work - work may not be performed on the basis of an agreement to perform work within a scope exceeding, on average, half of the set weekly working hours. Compliance with the agreed and maximum permitted scope corresponding to half of the set weekly working hours shall be assessed for the entire term for which the agreement to perform work was concluded, but not exceeding the term of 52 weeks.

While the contract of employment stands for basic and widespread form of the employment law relationship, the other two agreements, on work performed outside an employment law relationship, are only used as supplementary forms of the employment law relationship. The standard of special statutory protection of the employee's position based on the contract of employment is much higher in comparison with the level of protection under the other two agreements on work performed outside an employment law relationship (namely within agreements on work performed outside an employment law relationship, the employer is not obliged to distribute the employee's working hours). That is why the Labour Code stipulates that employers shall provide for the performance of their tasks particularly by employees in an employment law relationship. The two agreements on work performed outside an employment law relationship are considered as "dodgy" (or non-official) forms of employment, which are suitable for short-time seasonal jobs, various one-off assignments, occasional summer jobs etc.

Whether the work is performed based on a standard employment law contract or based on one of the other two supplementary agreements mentioned above, there are key characteristics, which are common for any form of dependant work. Factual dependent work may be performed only within an employment law relationship regulated by the Labour Code. This will not be altered by the title of the contract or other formal efforts of the contracting parties to stop the contract from being subsumed within the Labour Code.

The key characteristics of dependent work are as follows:

- the work is performed within a relationship in which the employer is superior and the employee is subordinate;
- the work is performed in the employer's name;
- the work is performed according to the employer's instructions; and
- the work is performed personally by the employee for the employer

The duty to subsume a legal relationship within the Labour Code and consider such a relationship "dependent work" based on all the above characteristics must be fulfilled cumulatively.

The consequences of the above key characteristics are that dependent work must be performed:

- for a salary, public sector pay or remuneration for work;
- at the employer's expense and responsibility; and
- during working hours at the employer's workplace or at another agreed place.

The assessment of key characteristics and consequences of dependent work implemented in concrete cases is rather demanding and may often lead to misinterpretation. For example, even though the subordination of the employee and employee's duty to follow the employer's instructions both stand for the key characteristics of dependent work, one must also take into consideration that even within common commercial relationships the duty to respect contractual conditions represents the usual nature of such non-employment legal relations (e.g. the duty to follow the coordinating client's instructions, the duty to submit to an inspection respecting technological procedures, work safety and fire regulations etc.). However, such contractual obligations may not be regarded as fitting the conceptual characteristics of subordination, which is typical for dependent work.

With respect to the above, the Supreme Administrative Court ruled that it is obvious that the obligation to fulfil the instructions occurs virtually in all situations, in which the work and/or activity has been assigned or ordered, i.e. not only within the frame of an employment law relationship. The definition of the statutory term "dependent work" cannot therefore be reduced only to legal relations/activities performed under the other's party instructions, but the dependent work shall be only the activity, which is truly dependent.²

As long as there does not exist a more detailed definition of the individual characteristics of dependent work, the true nature of the relationship between the two contractual parties must be identified in accordance with objective facts. If the activity of an individual in some aspects approaches the definition of dependent work within the meaning of the Labour Code, but is below its intensity, such legal relationship is not subsumed within the definition of 'dependent work' in terms of the Labour Code. As long as the legal relationship between the client and the self-employed worker/independent contractor does not cumulatively satisfy all the characteristics of dependent work, or excludes most of the defining criteria, such relationship cannot be considered as a 'dependent work' relationship.

The true nature of self-employed worker/independent contractor will be as a rule fulfilled if the self-employed worker/independent contractor:

- provides its services to more customers and does not have an exclusive relationship with just one customer;
- provides its services irregularly, i.e. not in precisely the same amount every week/

² <http://www.nssoud.cz/main0col.aspx?cls=JudikaturaSimpleSearch&SimpleSearch=1&cislofull=2%20Afs%2062/2004&pagesource=0>

- month;
- decides the place where the activity is carried out, i.e. has not been assigned the regular workplace at the customer's premises;
- delivers specialised and qualified activity, or an activity of a unique nature;
- performs activities, which are commonly performed outside employment law relationships;
- is entitled to remuneration, which relates to the factual provision of the services (amount, flexibility,... etc.) and may be modified with respect to outputs;
- the activity is carried out at the independent contractor's own expense (the independent contractor has his/her own equipment necessary for the provision of the services such as his/her own laptop, software, mobile phone ... etc.);
- does not present him/her-self as the client's employee;
- in relation to third parties, does not act in the client's/employer's name;
- performs his/her activities at times, which are not strictly stipulated by the client, for example has no standard "working hours";
- is not an integral part of an organisational chart of the client;
- is not subject to the binding instructions of the client's/employer's senior staff (besides the instructions in relation to control and inspection respecting technological procedures, work safety and fire regulations ... etc.);
- the client does not provide the independent contractor with personal protective equipment, work clothes and boots (including uniforms), washing, cleaning and disinfectant agents and protective beverages;
- the professional development is carried out at the independent contractor's own expense and within his/her free time;
- bears the burden of objective responsibility for damages. For example, with regard to third parties, and is eventually insured against these risks;
- in order to provide professional services has not been trained by the client (besides the initial trainings in relation to control and inspection respecting technological procedures, work safety and fire regulations ... etc.);
- is not regarded by third parties as the client's employee, i.e. is distinguishable from employees of the client (e.g. does not wear clothes with the logo of the customer, does not use business cards and email addresses of the client / customer etc.);
- requested the conclusion of commercial law relationship, i.e. was not interested in conclusion of employment law relationship; the commercial law relationship has not in any way been enforced by the client/ customer and fully meets the interests and desires of the self-employed worker/independent contractor;
- does not perform work, which is commonly performed by the client's employees;
- provides or may provide the services even through third parties (e.g. its own employees, subcontractors etc.), the services do not represent only personal performance of the activities; in case of an absence (e.g. due to temporary unfitness) the client does not substitute the independent contractor by its employee; and
- acts as an entrepreneur in terms of the Civil Code, i.e. as a person who, on his own account and responsibility, independently carries out a gainful activity in the form of a trade or in a similar manner with the intention to do so consistently for profit.

b. General Differences in Tax Treatment

Conclusion of an employment law relationship (employment law contract, the agreement to complete a job or the agreement to perform work), as well as a civil law contract, gives rise to obligations of payment of the personal income tax advance to the tax office and payment of contributions to the Czech Social Security Administration (CSSA).³ The amount and type of deductions from the employee's remuneration depends on the type of contract concluded.

Employment law contracts

Income from dependent work includes income and related remuneration from employment. In the Czech Republic, an employee pays 15% Income Tax with an additional 7% solidarity tax surcharge (hence in total 22%), which applies to employees making more than 48 times the average salary (1,355,136 CZK;⁴ about EUR 50,000) annually.

Pensions are operated by the CSSA and are made up of salary based contributions paid by both the employer and the employee. Receipt of pension benefits is contingent upon payment of the social security contributions (Act No. 589/1992 Col., on Premiums for Social Security and Contribution to the State Policy of Employment, as amended). Employees currently contribute 6.5 percent of their taxable income to social security schemes, while employers contribute 25 percent of the gross taxable income of all its employees. Sickness insurance is an integral part of Social Security; participation in sickness insurance by an employee is mandatory under the law.

Health insurance contributions amount to 13.5 percent of an employee's gross taxable income; one third (4.5 percent) of which, is paid by the employee and the remaining two thirds (9 percent) by the employer. There is a new maximum calculation base for payment of social security contributions and contribution to the state employment policy, defined as 48 times the average annual wage. The maximum calculation base for the purpose of insurance premium calculations amounted to CZK 1,355,136 in 2017.

Civil law contracts – independent contractors

In contrast to income gained through employment law relations, the overall taxation of self-employed workers/ independent contractors is lower. This is because all taxes and contributions are paid solely by the independent contractor and are therefore exempt from the employer's contributions as explained in the previous section. The independent contractor pays 15% Income Tax with an additional 7% solidarity tax surcharge (hence in total 22%)

If the statutory conditions are satisfied, participation in pension insurance and the payment of a contribution to the state employment policy are mandatory for independent contractors. An independent contractor participates in pension insurance: applies for contractors making more than 48 times of the average salary (1,355,136 CZK;⁵ about EUR 50,000) annually.

If the statutory conditions are satisfied, participation in pension insurance and the payment of a contribution to the state employment policy are mandatory for independent contractors. An independent contractor participates in pension insurance:

- in a calendar year for the period in which he/she carried out a major independent gainful activity;
- in a calendar year for the period in which he/she carried out a subsidiary independent

³ <http://www.cssz.cz/en/about-cssa/>

⁴ http://kalkulacky.idnes.cz/cr_kalkulator-osvc-2017.php

⁵ http://kalkulacky.idnes.cz/cr_kalkulator-osvc-2017.php

- gainful activity, if the income from the subsidiary independent gainful activity, after deducting expenses, reached the so-called decisive amount; and
- in a calendar year for the period in which he/she carried out a subsidiary independent gainful activity, if he/she registered for participation in pension insurance.

Pension insurance premiums must be paid by every independent contractor who, in the preceding year, carried out a major independent gainful activity. The premiums are 29.2% of the assessment base. The independent contractor him/herself determines the amount of the annual assessment base for premium payments. The lowest assessment base is determined as 50% of the tax base (under the Income Tax Act). The minimum assessment base is amended each year by a Decree of the Government and differs for major and subsidiary independent gainful activity. In both cases, the months during which the self-employed person was entitled to sickness benefits for the whole month from the sickness insurance scheme for self-employed persons, or was granted maternity benefits in cash, or carried out military service are not included in this number of calendar months.

The maximum (annual) assessment base for self-employed persons for pension insurance premiums and the contribution to the state employment policy is 72 Zmes the average wage. This assessment base for self-employed persons is not reduced by the proportional part.

Unlike employment law relations participation in sickness insurance by independent contractor is voluntary under the law.

c. Differences in Benefit Entitlement

All employee benefits are regulated by the Labour Code and related Governmental Decrees. Additional entitlements may also be granted to employees by the collective agreements and internal regulations issued by an employer. The additional entitlements may stipulate rights in employment law relationships that are more favourable for the employees than the rights stipulated in the Labour Code. More favourable rights can also be granted to employees based on individual contracts of employment (typically through employment contracts with senior employees).

Only employees are guaranteed traditional statutory protection, which permeates the entire Labour Code. For example, an employer may give notice to an employee only on the statutory grounds; an employee is entitled to statutory leave (minimum four weeks); maximum full-time weekly working hours is 48 hours per week, including overtime; an employee is entitled to statutory extra payments (for overtime work, for work on holiday, for work on Saturdays and Sundays, for Work in Unfavourable Working Environment, ...); and severance pay in cases where the employer terminates the employment contract by giving notice, on the grounds of organisational changes or unfitness to perform the current work due to an accident at work or occupational disease.

In contrast, independent contractors performing “work”, by providing services based on a civil law contract have no rights to any employee entitlements based on labour law. This is in line with the fact that independent contractors are covered neither by the Labour Code nor by other sources of labour law. It implies that the above benefits (such as annual time off, extra payments for service delivery at weekends, severance pay in case of termination of the contract etc.) are only available to independent contractors if they have negotiated it into their contract. For these purposes, the mandate-type contracts (Sec. 2430 et seq. of the Civil Code) or innominate-type contracts (Sec. 1746 part. 2 of the Civil Code) are usually concluded with independent contractors.

On the condition that an independent contractor contributes to the social security

system, they may benefit from the same range of social security benefits, which are awarded to employees. Pensions in the Czech Republic are operated by the CSSA and are made up of salary based contributions paid by both the employer and the employee, as well as contributions paid by self-employed individuals/independent contractors. The CSSA is responsible for deciding who is entitled to pension benefits and the amount awarded to entitled individuals. The CSSA bases its decision on an application, which is submitted to the local District Social Security Administration OSSZ/PSSZ/MSSZ, pursuant to the place of the applicant's permanent residence. If an applicant does not have a permanent residence in the Czech Republic, any OSSZ/PSSZ/MSSZ in the Czech Republic can fill in the application.

The following benefits are provided to employees as well independent contractors from pension insurance if the following conditions are fulfilled:

- old-age pension;
- invalidity pension;
- widow's and widower's pension; and
- orphan's pension.

Maternity leave

Following childbirth, a female employee is entitled to maternity leave for a period of 28 weeks; if the employee gives birth to two or more children at the same time, she is entitled to maternity leave for a period of 37 weeks. Maternity leave in connection with childbirth can never be shorter than 14 weeks and cannot be terminated or interrupted prior to six weeks from the date of the birth.

A basic condition for entitlement to financial assistance while on maternity leave is participation in insurance (e.g. continuation of insured employment) at the time of commencement of maternity leave (financial assistance during maternity). A woman who commences maternity leave after leaving work but within the period of protection is also entitled to the benefit. The period of protection for women whose insurance (employment) terminated during pregnancy is 180 calendar days from the date of termination of the insurance. The insured person must have participated in the sickness insurance scheme for at least 270 calendar days over the last two years before the date of starting the maternity leave to have the right to this benefit.

Sickness

From 1 January 2014 an employee is entitled to sickness benefits from the insurance company after the 15th calendar day of his/her temporary incapacity to work. During the first two weeks of the temporary incapacity to work, an employer will provide the employee with a compensation wage for working days; however, compensation for wages, salary or remuneration will not be paid for the first three days of this period. The employee will only be entitled to a compensation wage for the period of the employment relationship that establishes the participation in sickness insurance. The support period lasts no longer than 380 calendar days from the date of the temporary incapacity to work or quarantine order, unless stated otherwise. The amount of sickness benefit per calendar day is 60% of the reduced daily basis of assessment.

In the Czech Republic independent contractors can voluntarily choose whether to participate in sickness insurance or not. If the independent contractor does participate in sickness insurance, he may be entitled to sickness benefits from the insurer, under the same conditions outlined above.

d. Differences in Protection from Termination

As explained above, the high standard of statutory protection under the Labour Code

applies exclusively to parties of an employment relationship. They do not apply to civil obligations. This also refers to the conditions of terminating contracts of employment.

Protection from Termination – Employment Contracts

While an employee may give notice to an employer on any grounds or without stating the grounds, an employer may only give notice to an employee on the following grounds (employer's notice of termination given without grounds or on the bases of different grounds will be void):

- if the employer or part thereof is being dissolved;
- if the employer or part thereof is being relocated;
- if the employee becomes redundant given a decision of the employer or the competent body on a change in his/her tasks, technical equipment, reduction of the personnel for the purpose of increasing work effectiveness or other organisational changes;
- if the employee may not further perform the current work due to an accident at work, occupational disease or threat of such a disease based on a medical report issued by a provider of occupational health services or a decision of the competent administrative authority reviewing such a medical report, or if the maximum permissible exposure of the employee has been reached at the workplace based on a decision of a public health protection body;
- if the employee is deprived of his/her medical fitness in the long term, given his/her state of health based on a medical report issued by a provider of occupational health services or a decision of the competent administrative authority reviewing such a medical report;
- if the employee fails to fulfil the prerequisites stipulated by the legal regulations for the performance of the agreed work or if the employee fails to fulfil the proper performance requirements of the agreed work. If non-fulfilment of these requirements is based on unsatisfactory working results, the employee may be given notice on these grounds, but only if the employee has been requested by the employer, in writing, to provide a remedy during the last 12 months and the employee has failed to provide for a remedy within an appropriate deadline;
- if the employee acts in such a way which enables the employer to terminate the employment contract by immediate termination, or that gives rise to gross breach of a duty arising out of legal regulations, then an employee may be given notice on the basis of a regular, less serious breach of duty. Notice will be given if the employee has been advised, in writing, of the possibility of being given notice in relation to a breach of duty which took place within the last six months; and
- if the employee commits a particularly gross breach of any other of his/her duties stipulated in Section 301a. Examples of such an act include; the duty to observe during the first 14 calendar days the regime of an insured person who is temporarily unfit to work and in respect of the obligation to stay at his/her place of residence and comply with the time and scope of permitted absence from home pursuant to the Sickness Insurance Act at the time of temporary unfitness to work.

Dismissal must be given in writing otherwise it will not be valid. An employer must specify the relevant grounds in the notice so that they cannot be confused with any other grounds. The grounds for the notice may not be subsequently changed. Dismissal given by an employer may be withdrawn only with the employee's consent; both the withdrawal of the notice and the consent to withdraw the notice must also be stipulated in writing.

It is prohibited to give notice to an employee during the period of protection, for example:

- at a time when the employee is found temporarily unfit to work, unless he/she has intentionally caused such unfitness or unless the unfitness arose as a direct consequence of the employee's drunkenness or abuse of addictive substances;
- in the performance of a military exercise or an extraordinary military exercise;
- at a time when the employee is fully released for the discharge of a public office for a long term;
- at a time when a female employee is pregnant or when a female employee is on maternity leave or when a female or male employee is on parental leave; and
- at a time when an employee working at night is found temporarily unfit to perform night work based on a medical report issued by a provider of occupational health services.

Protection from Termination – Civil Law Contracts

Independent contractors, who provide services based on a civil law contract, have no right to any increased protection against unilateral termination. This corresponds with the fact that mandate-type contracts or innominate-type (not named) contracts are subsumed within the Civil Code; unless explicitly agreed otherwise, they apply only basic rules for termination of any common civil law contract. This means that in practice, unless the contract states otherwise, a mandate-type contract or an innominate-type contract could be terminated overnight.

Unless agreed otherwise, a client may withdraw a contractor's agreement at any time; however, she/he shall compensate the contractor for the costs, which she/he has incurred until that time and, where applicable, for any damage incurred, as well as remuneration for work already undertaken in line with the agreement.

If a civil law agreement between the independent contractor and his client is concluded for an indefinite period, and obliges at least one party to perform a continuous or recurrent activity, or obliges at least one party to tolerate such an activity, the obligation can be stopped at the end of a calendar quarter by giving at least three months' notice of termination.

e. Local Limitations on Use of Independent Contractors

As long as a civil law contract is not intended to disguise a genuine employment relationship, there are no limitations in the Czech Republic regarding the use of civil contracts. The contracting parties are free to choose the contract-type. Mandate-type contracts (Sec. 2430 et seq. of the Civil Code) or innominate-type contracts (Sec. 1746 part. 2 of the Civil Code) are usually applied for legal relations concluded with independent contractors. The statutory provisions of the Civil Code governing various types of contracts apply to contracts whose contents include the essential elements of a contract provided under the basic provision for each of those contracts. Parties may also conclude a contract that is not specifically regulated as a type of contract.

If a civil law contract is intended to obscure a factual employment contract, the former is assessed according to its true nature. Therefore, replacing a contract of employment with any civil law contract, (while meeting the usual criteria of labour employment), actually represents an administrative offence. A fine of between CZK 50,000 (EUR 1,900) and CZK 10,000,000 (EUR 370,000) can be awarded for such an offence. Moreover, a factual employer would also take responsibility for any health insurance and social security contributions, including the duty of payment of overhead surcharges, related interests and sanctions.

f. Other Ramifications of Classification

Other ramifications of classification of individuals as self-employed workers/independent

contractors relate to their reduced level of protection in comparison to the traditionally high levels of protection awarded to employees. For example, only employees enjoy the following increased legal protection:

- the amount of the requested compensation for damage caused by an employee's negligence may not exceed four and half times the amount of the employee's average monthly earnings prior to breach of the obligation whereby the damage was caused. This limitation shall not apply if the damage was caused intentionally, under the influence of alcohol or arer abuse of other drugs. The amount of the requested compensation for damage caused by an independent contractor is without any limits;
- an employer is obliged to compensate an employee for damage or non-material damage, which arose due to an accident at work. The damage or non-material damage must have happened during the performance of a working task or in direct connection therewith. On the other hand, the independent contractor's client takes no responsibility for an independent contractor's accidents at work;
- unless negotiated explicitly otherwise, an independent contractor's civil contract may be terminated on any grounds (not only on the statutory grounds, such as organisational changes), whereas an employee is entitled to statutory leave (minimum four weeks). There is no limit on maximum full-time weekly work with regard to independent contractor; the independent contractor is not entitled to any paid leave... etc.;
- most of the safety regulations, such as those regarding the prevention of accidents at work, are not applicable to independent contractors;
- the right to organise themselves in trade union units; only employees may be represented by a trade union and/or works council, including the exercise of the extensive right to information and consultation;
- return of monies paid without justification may be demanded by the employer from the employee but only if the employee knew or must have assumed, under the given circumstances, that these amounts were determined incorrectly or paid out erroneously, and the employer may so demand within three years of the day of their payment; and
- during court disputes, the below basic principles of employment law relationships must be applied as an interpretation rule for employees.

The meaning and purpose of the provisions of the Labour Code are expressed by the basic principles of employment law relationships, which are, in particular,

- special statutory protection of the employee's position;
- satisfactory and safe conditions for the performance of work,
- just remuneration of the employee;
- proper performance of work by the employee in accordance with the legitimate interests of the employer; and
- equal treatment of employees and prohibition of discrimination against them.

g. Leased or Seconded Employees

Under Czech law, it is possible to:

- temporarily assign employees to another employer; or
- lease employees through employment agency. Temporary assignment

An agreement on the temporary assignment of an employee to another employer can be concluded arer six months from the commencement of the employment law relationship.

No consideration can be provided for temporary assignment of an employee to another

employer. If the employer is a legal entity, the agreement must state; the employer's trade name that the employee is being temporarily assigned to, the date of commencement of the temporary assignment, the type of work to be performed, the place of work and the time for which the temporary assignment is agreed. The agreement may also stipulate the regular workplace for the purposes of travel allowances. The agreement must be concluded in writing.

During temporary assignment, the temporary employer is responsible for providing work to the employee, as well as organising, managing and controlling his/her work, giving him/her binding instructions, creating favourable working conditions and providing occupational health and safety protection. A temporary employer is not entitled to take legal actions in relation to the temporarily assigned employee on behalf of the employer that temporarily assigned the employee.

During temporary assignment, the temporarily assigned employer shall pay the employee's salary and, if appropriate, travel allowances. The working and salary or public sector pay conditions of the temporarily assigned employee must not be worse than they are or would be under the conditions of a comparable employee of the employer, to which the employee has been temporarily assigned.

"Leasing" of employees through employment agency

Czech law allows employment agencies to temporarily assign an employee to another employer, on the basis that:

- authorisation pursuant to Act on Employment is provided;
- in accordance with the employment contract or agreement between the employee and agency, it is agreed that the agency is able to secure temporary work for an employee; and
- the employee undertakes a duty to perform work according to the user's instructions.

During the temporary assignment of an employment agency's employee, the temporary employer will impose working tasks on the employee as well as; organising his/her work, managing and controlling the employee, giving the employee instructions, creating favourable working conditions and providing occupational health and safety protection. However, the temporary employer may not bring legal action in relation to the employee of the employment agency on behalf of the employment agency.

The employment agency and the temporarily assigned employer shall be obliged to ensure that the working and payment conditions of a temporarily assigned employee are not worse than the conditions or potential conditions of a comparable employee. If the working or payment conditions of a temporarily assigned employee are worse during the term of performance of work for the user, the employment agency shall be obliged, at request of the temporarily assigned employee, or if it ascertains this fact otherwise, even without request, to provide equal treatment. The temporarily assigned employee shall have the right to claim the satisfaction of the rights incurred against the employment agency.

An employment agency may not temporarily assign the same employee to the same user for a term exceeding 12 consecutive months. This limitation does not apply in cases where this is requested from the employment agency by an employee of the employment agency or in respect of the performance of work for a period of replacing a female employee who is on maternity leave or parental leave, or for a male employee who is on parental leave.

h. Regulations of the Different Categories of Contracts

In contrast with many other countries, Czech labour and employment law is consolidated into a single Labour code, which is accompanied by other national legislation, judiciary and collective bargaining agreements. Therefore, under Czech law, contracts with independent contractors (including conclusion, termination of a contract, its content, form, interpretation of a contract, limitation periods ... etc.) are governed by the Civil Code.

Many of the employment protective regulations constitute a mandatory minimum; a derogating (or divergent) regulation of rights or obligations in employment law relationships must not be lesser or greater than the right or obligation stipulated by the Labour Code or the collective agreement as the least or most admissible. If an employee waives a right granted to them by the Labour Code, collective agreement or internal regulation, such waiver shall not be valid. Conversely there are scarcely any binding rules regarding terms and conditions for the engagement of independent contractors.

In the past three years, the Czech Republic's employment law has been significantly affected by reform to the Czech civil law, which came into effect 1 January 2014. After 50 years, the former Civil Code (dated 1964, which was adopted in the communist era), was replaced by the entirely new Civil Code (Act No. 89/2012 Coll.). This change represents the most conceptual change in the field of law since the Velvet Revolution in 1989, and probably the most extensive change in legal thinking and interpretation in the past 50 years. It is natural that such a profound change brings a certain level of chaos in relation to experienced orders, including the necessity of companies and individuals to adjust to "new orders". For example, the reform of the Civil Code brought new regulations into the conclusion of a contract, the interpretation of a contract, limitation periods, new in the form of "offer letters", as well as "expectation damages" etc.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Regardless of the title of the contract or other formal efforts of the contracting parties to avoid the contract being subsumed within the Labour Code, factual dependent work may be performed only within an employment law relationship regulated by the Labour Code.

If a civil law contract is intended to obscure a factual employment contract, the former is assessed according to its true nature. Therefore, the replacement of the contract of employment by any civil law contract, while factually meeting the usual criteria of labour employment, represents an administrative offence. If such an offence is committed the factual employer may be fined between CZK 50,000 (EUR 1,900) and CZK 10,000,000 (about EUR 370,000). Moreover, the factual employer would also take responsibility for consequences in the area of health insurance and social security contributions, including its duty of payment of overhead surcharges, related interests and sanctions.

b. The Legal Consequences of a Re-Characterisation

Reclassification risk is typically when governmental authorities determine that an independent contractor is actually an employee; although this may stem from the contractor him/herself. If the contractor is reclassified as a *Hays (global specialist recruitment group)* employee, the following consequences shall be considered:

Unpaid taxes

According to Czech law, contractors can only be self-employed individuals, if the self-employed individual's turnover exceeds CZK 1,000,000 in the past 12 or less calendar months. The self-employed individual is obliged to register as a VAT payer and will be automatically subject to VAT. In the case of self-employed individuals, the client (factual employer) pays the fees gross and the independent contractor will be responsible for payment of their own taxes, including, premiums for social security and general health insurance. If self-employed workers/independent individuals are reclassified as employees, then their "factual employer", becomes responsible for the additional payment of employment-related taxes. The tax authorities will consider the Contractor's fee (which was until then paid to him by factual employer) as "net salary" (no matter the fact the contractor himself had already paid all taxes incl. social/health insurance from such a fee); therefore the tax authority will first re-calculate the "net salary" up to "gross salary" (plus another 34%); and only from this new tax base (i.e. original fee + 34%) the tax authority will assess the new tax duty.

The above practice in fact represents double taxation, but in this specific situation double taxation is allowed by law and even by court practice. Moreover the factual employer would pay taxes and social/health insurance from tax base, which is 34% higher than the original fee. In other words, in cases of re-classification the factual employer would be obliged to pay more than double the original fee paid to the "contractor" (now employee). On top of that, the tax authority would impose a penalty (another 20% of the new tax duty) and an interest of late payment (another 14.5 % annually).

Overtime

Reclassifying the contractor as an employee could result in additional (up to 25%) overtime being payable; given that the contractor would not have been eligible for overtime as well as liability for employment related claims, such as damages for unlawful dismissal, etc. If the contractor is reclassified as an employee, she/he could sue the factual employer for any damages incurred as the result of such re-classification.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Even though the authority's judicial decision may be challenged by either party, it is usually the individual ("independent contractor"/employee) who initiates the legal proceedings. The independent contractor/employee often feels somehow aggrieved by the fact that his/her civil law contract was concluded to intentionally obscure a factual employment contract. Such an individual may submit an action to the civil court and sue straight away for performance arising from regular employment law relations (e.g. the performance arising from invalid termination, failure to provide for the salary, travel allowances, holiday etc.). If the plaintiff's argument prevails, the court will determine that an employment relationship is in place, and/or has been concluded sometime in the past between the employee and the employer. At the same time, the court may grant a successful plaintiff money or other remedies which are actionable at court proceedings. If it is a dispute about termination, the court may even determine that the termination of the contract is invalid.

Besides civil courts, there may also be judicial remedies at administrative courts. These take place when either an "independent contractor"/employee or administrative bodies (social security⁶, health insurance companies⁷) doubt an "independent contractor's" social status (e.g. with regard to the entitlement to the provision of any form of pension, sickness/maternity benefit, attendance allowance, compensatory benefit in pregnancy and maternity etc.).

⁶ <http://www.cssz.cz/en/about-cssa/>

⁷ <https://www.vzp.cz/>

The decisions made by the courts are not easy to predict since accurate differentiating of employees from self-employed workers/independent contractors represents a legally difficult task, even for courts. There are often only subtle differences, which speak either for a contract of employment or a civil law contract. Therefore, the cases at civil and administrative courts differ from one another. The courts make their decisions depending on the circumstances of individual cases and it will be a few more years before the Czech judiciary stabilise and enable unifying conclusions in the area to be made.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

As already mentioned above, replacing a contract of employment with any civil law contract, (while meeting the usual criteria of labour employment), actually represents an administrative offence, for which the bodies responsible for inspection of work may impose on the factual employer a fine up to CZK 10,000,000 (about EUR 370,000), but not less than CZK 50,000 (EUR 1,900).

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Employment law regulations that ensure the increased level of protection of employee's status (such as obligatory written form of the contract and termination, obligatory written form of records stating the beginning and end of working hours etc.) do not apply to self-employed individuals / independent contractors.

Under Czech law, it is not mandatory to conclude a civil law contract with an independent contractor (most frequently mandate-type or innominate contract) in writing but in practice it is highly recommended to do so in order to prevent unnecessary litigation. If there is a service agreement with an independent contractor, it should include typical provisions of an independent contractor's contract (see below) as well as being free of any provisions typical of an employment relationship.

The basic limitation period in the Czech Republic is three years and so it is highly recommended for individual independent contractors that are within the three year limitation period to keep the following documentation; outputs of the services provided, all invoices, documents certifying that the independent contractor organised himself the working hours, further the declarations from the independent contractor, the contractor's business card as well as any references on the contractor's marketing activities etc.

b. Day-to-Day Management of the Relationship

Regarding the day-to-day management of the relationship with the independent contractor, it is crucial to observe, among others, that the independent contractor:

- provides its services, if possible, irregularly, i.e. not in precisely the same amount every week/month;
- shall be given a deadline when a concrete project must be finished rather than being obliged to follow the beginning and end of the "shifts" as determined by the client;
- shall be relatively free regarding the choice of place where the activity is carried out, i.e. has no regular workplace at the customer's premises;
- is entitled to remuneration, which relates to the factual provision of the services

- (amount, flexibility,... etc.) and may be modified with respect to outputs;
- the activity is carried out at the independent contractor's own expense (the independent contractor has his/ her own equipment necessary for the provision of the services such as his/her own laptop, software, mobile phone ... etc.);
- is not an integral part of an organisational chart of the client;
- the professional development is carried out at the independent contractor's own expense and within his/her free time;
- bears the burden of objective responsibility for damages, e.g. with regard to third parties, and is eventually insured against these risks; and
- is not regarded by third parties as clients' employee, i.e. is distinguishable from employees of the client (e.g. does not wear clothes with the logo of the customer, does not use business cards and email addresses of the client / customer etc.).

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The use of independent contractors represents a complex issue in relation to uncontrolled developments of information technologies. The question about how employment, civil and administrative law will react to future trends, which involve replacing traditional employment relationships with common civil law relations is being asked, not only within the Czech Republic, but globally as well. Such trends may have been medially provoked by "independent" UBER taxi drivers, but the real trends are much more deeply entrenched and are now expanding to almost any activity performed by an individual for remuneration.

With respect to general absence of clear unifying examples from the judiciary or labour inspection, which would doubt the use of independent contractors, it is expected that the use of independent contractors to perform a company's tasks might further expand.

b. Recent Amendments to the Law

So far the latest relevant amendment to the employment law was implemented with effect from 1 January 2012. Since then the replacement of an employment contract by a civil law contract while factually meeting the usual criteria of labour employment officially represents an administrative offence, for which the bodies responsible for the inspection of work may impose on the factual employer a fine up to CZK 10,000,000 (EUR 370,000), but not less than CZK 50,000 (EUR 1,900).

The introduction of the new Civil Code, which came into effect on 1 January 2014, represents the latest change in the field of civil law. The Civil Code is liberal and does not prohibit the use of independent contractors. The introductory provisions stipulate that unless expressly prohibited by a statute, persons can stipulate rights and duties by way of exclusion from a statute; stipulations contrary to good morals, public order or the law concerning the status of persons, including the right to protection of personality rights, are prohibited.

Since 2012/2014 there have not been any relevant amendments to the law regulating the status of independent contractors and at the moment there are not even any new amendments being prepared.

VI. CONCLUSION

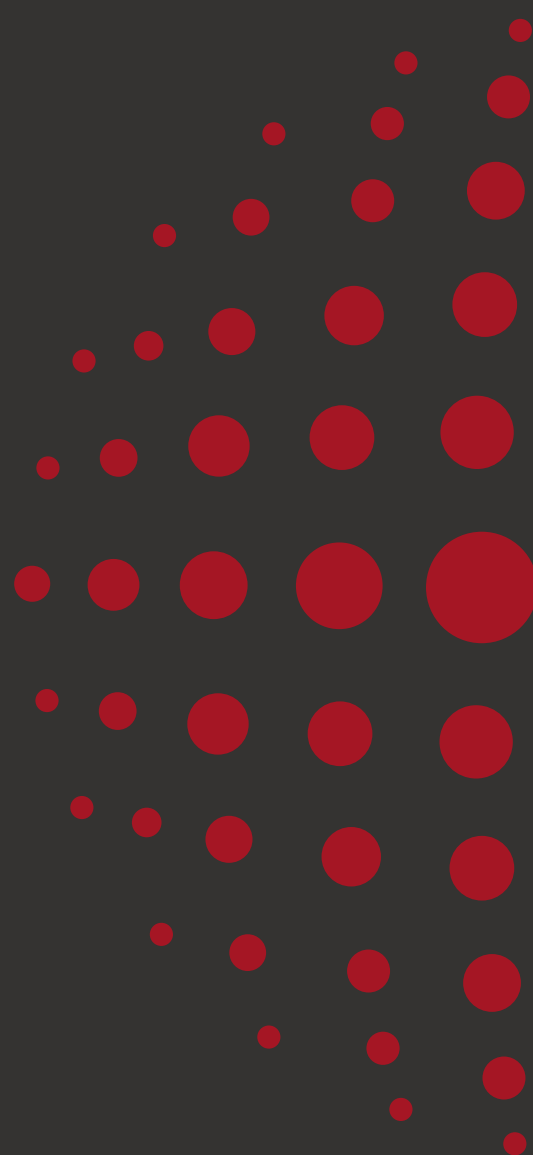
Under the Czech Republic law, as long as a civil law contract is not intended just to obscure a factual employment contract, there are no limitations in relation to the use of civil contracts. The contracting parties are even free to choose the contract-type. At the same time, it must be noted that the use of self-employed workers/independent contractors is not suitable for every activity. There exist substantial differences between the legal correctness and defensibility of the use of self-employed workers/independent contractors within various sectors.

While it might be relatively easy to structure and defend the necessity of a civil law contract concluded with the independent contractor, who provides external support such as; IT specialist, external interpreter, external marketing, PR, administrative support, all sorts of external consultancy services etc., it is hardly arguable to defend a civil law contract concluded with workers in “traditional” sectors such as; industry, construction, salesmen in the shop, health-care workers etc.

In other words, under existing Czech law the use of self-employed workers/independent contractors fits and is much more defensible in relation to activities with a predominantly intellectual value added compared to traditional areas with a predominantly manual and/or strictly organised workforce.

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DENMARK

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I. OVERVIEW

a. Introduction

Denmark has never adopted a general employment “constitution” so, unfortunately, there is no general rule, which can be applied to determine whether a person is an employee or an independent contractor. Instead, the Danish courts have handed down judgements giving specific rules on, for example, holiday entitlement, the issuing of employment certificates, withholding tax and other mandatory rules. In essence, there are a number of factors, which determine whether a person is an employee or an independent contractor, but certain factors are more significant than others.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

A worker who has an employment contract is considered as an employee. There are three essential elements creating an employment contract: Personal work, remuneration and "relationship of authority". The third element is the most significant. An independent contractor is a person (or a company) performing professional activities in respect of which he/she is not bound by an employment contract; this means that he/she does not work under the authority of an employer. Consequently, it is the lack of subordination, which distinguishes an independent contractor from an employee so that if one of these parties exercises an employer's authority over the other, the relationship will be considered an employment contract.

If a Danish court is required to decide whether a person is an employee or an independent contractor, the court will consider:

- if the person carrying out work is in a subordinate position and takes instructions and works under supervision/control from a manager;
- which party is responsible for the result of the work performed;
- if the person carries out work for only one contractor or if he/she has other customers;
- does the person fulfill his/her work obligations regularly and using the same methods of work as ordinary employees employed by the contractor, including if the person has fixed working hours, makes use of working tools owned or facilitated by the contractor, makes use of the contractor's canteen facilities, participates in social activities available to the contractor's employees, etc.?
- if the person must personally perform the work or if he/she can designate the work to another person;
- if the person runs a personal financial risk when carrying out work for the contractor;
- if the person has established his/her own independent business registered with the Danish Business Authority.

b. General Differences in Tax Treatment

Income tax

For an employer doing business with an independent contractor, payment of the agreed fees will be made directly to the independent contractor without deducting any tax and with the addition of VAT (25 %) on the contractor's fees. Thus, the independent contractor is personally responsible for the payment of taxes and VAT to the Danish Government. Within the framework of an employment contract, the employer is obliged

to withhold tax at source.

Furthermore, the independent contractor must file an annual tax account (turnover deducted with all business related costs, declaring appreciations on business assets and interest paid) to the Danish tax authorities, while the employee will only file a summary tax return form as the employer will report almost all important information related to the remuneration earned by the employee to the Danish tax authorities.

The level of income tax for independent contractors and employees is similar. The income tax level is progressive – the higher the income, the higher the tax level, ending in a maximum tax level of approximately 60% per cent, but the independent contractor may benefit from certain tax advantages, such as the ability to deduct business related costs.

Pension and Supplementary Pension Contributions

Under Danish law, it is not mandatory for employers to give employees access to a pension scheme. However, quite a number of individual employment agreements and, in general, all collective bargaining agreements will involve the payment of supplementary pension contributions, both by the employer and by the individual employee to a pension labour market pension scheme. The level of labour market pension contribution is solely a contractual matter and not set by legislation. Apart from pension schemes involving civil servants, a Danish labour market pension scheme will be a “defined-contribution” pension scheme. The employer of an independent contractor is obliged to, and cannot make pension contributions to the independent contractor’s privately established pension scheme.

An employer is responsible for the declaration and payment of both the employee’s and the employer’s supplementary pension contributions in accordance with the Danish Act on Labour Market Supplementary Pension (Act no. 1110 of 10 October 2014), which provides that employers and employees must contribute to a Governmental supplementary pension scheme, for employees who are employed in Denmark. The employer’s contribution is a fixed monthly payment of approximately EUR 40 covering a fulltime employee and the employee’s contribution approximately EUR 20. The supplementary pension is paid out in addition to the Governmental old-age pension scheme. The employer of the independent contractor is not bound to make contributions to the Labour Market Supplementary Pension on behalf of the independent contractor.

c. Differences in Benefit Entitlement

Independent contractors are not entitled to specific benefits; they only receive the fees agreed between the parties with the addition of VAT (25%).

Apart from the agreed salary and benefits, employees are entitled by law to the payment of either holiday pay (12.5% of the salary and all taxable benefits) or salary during five weeks' holiday per holiday year, and salary or state sickness benefits during periods of sickness.

d. Differences in Protection from Termination

The way in which contractual relationships are terminated is the same for contracts covering the relationship between contractors as it is for termination of other forms of independent contracts, which means the parties are free to agree whatever terms they wish.

For employees, there are a set of rules restricting the termination of the employment of employees and such rules are based on either mandatory legislation or on individual or collective agreements. As a general rule, an employee cannot object to being dismissed,

neither can trade unions or governmental bodies. However, certain procedures may be provided for according to collective agreements. If a dismissal is not made on fair grounds, the employee may be entitled to compensation for unfair dismissal.

A number of employees enjoy special protection against dismissal (e.g. pregnancy, paternity or parental leave, position as shop steward or safety steward, complaints against unequal treatment, etc.). The rules providing this special protection are derived from legislation or collective agreements. Depending on the specific case, the protection requires certain procedures to be followed prior to the issuing of the notice of dismissal.

e. Local Limitations on Use of Independent Contractors

There are no limitations on the use of independent contractors, but they must register as “business owners” with the Danish Business Authority and with the tax authorities.

f. Other Ramifications of Classification

Where an employer's business is closed down, employees can benefit from the intervention of the “Employees’ Guarantee Fund” (Lønmodtagernes Garantifund, “LG”). The LG is mainly financed by the Danish Government, by employers’ contributions and reimbursements by receivers and liquidators of the amounts that were paid in advance to the employees. In practice, the LG pays the amounts payable to the employees and recovers them afterwards from the receivers and liquidators. The LG supports employees in case of bankruptcy, insolvent liquidation and business closure.

Following certain legal criteria, the LG makes different kinds of payments to the employees: Closing-down indemnities, contractual indemnities, pension contributions, bonuses, holiday allowance, and severance payments based on legislation and on certain collective agreements.

g. Leased or Seconded Employees

A “lease” of employees can only be arranged through temporary work agencies, namely an agency for the purpose of hiring out their employees to other companies in need of extra workers. However, these companies will not become employers to such temporarily employed employees, but will instruct them in their day-to-day work during the ‘lease’ period.

“Leased employees” are protected by the Danish Act on Temporary Work (Act no. 595 of 12 June 2013), which provides that the hired employees are entitled to the same level of salary, benefits and working conditions as if they were employed directly by the company hiring them.

A secondment of employees will typically only take place through an agreement entered between the seconded employee, the employer and the company to which the employee will be seconded, typically for a limited period of time.

h. Regulations of the Different Categories of Contracts

In Denmark, employment relationships are regulated through legislation, collective bargaining agreements or individual agreements. However, all employment relationships (provided they exceed one month's duration and the employee works on average more than eight hours per week) must adhere to the mandatory Danish Act on Employment Contracts (Act no. 240 of 17 March 2010). This Act regulates terms and conditions of employment and sets out what clauses must be included in an employment contract, such as salary and benefits, holiday entitlement, notice period, place of work, whether

the employment is covered by a collective bargaining agreement, etc.

Finally specific rules apply to particular groups of employees, such as the Danish Act on Seamen (Act no. 73 of 17 January 2014), the Danish Act on Civil Servants' Rights (Act no. 488 of 6 May 2010) and the Danish Act on Farming and Household Assistants (Act no. 712 of 20 August 2002).

In comparison, agreements entered into with independent contractors are not regulated and there are no Acts which regulate the engagement of independent contractors. Instead, the general civil, commercial and corporate laws will apply to an independent contractor agreement.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

A re-characterization of an independent contractor may occur if the person performing the work is deemed to be an employee, for example in terms of the Act on Employment Contracts, the Holiday Act or the Salaried Employees Act. A re-characterization of an independent contractor as an employee may also take place if the tax authorities conclude that the payment for services under the contract with an independent contractor in reality, is payment for work performed under an employment relationship.

For example the Danish Holiday Act Section 1.2 (Act no. 1177 of 9 October 2015) defines an employee as follows:

"For the purpose of this Act an employee shall be taken to mean a person receiving remuneration for personal work in an employment relationship."

As the wording of the above definition may be considered "circular" and no general rule exists in Danish legislation to assist with defining an employee or an employment relationship, a re-characterization can only be made by the Danish courts after an in-depth analysis of how the parties interacted with one another. The courts will consider a number of factors, but the most important guiding principles to determine if work was carried out by an employee or an independent contractor will be the following criteria:

- if the person carrying out work is subordinate, takes instructions and works under the supervision/control of a manager;
- if the person regularly or perhaps even on a daily basis carries out work for the same employer and typically works for only one employer;
- if the person carries out work for only one employer or if he/she has other customers;
- if the person fulfills his/her work using the same working methods as ordinary employees employed by the employer, including if the person has a fixed number of working hours, makes use of tools owned or provided by the employer, makes use of the contractor's canteen facilities, participates in social activities available to the employer's employees, etc.
- if the person is required to perform the work personally and is not allowed to delegate the work to another person;
- if the person is responsible for the outcome of the work;
- if the person runs a personal, economic risk when carrying out work for the employer; and
- if the person has established his/her own independent business, registered with the Danish Business Authority and the tax authorities.

b. The Legal Consequences of a Re-Characterisation

In the event of re-characterization, there are several legal consequences regarding employment, tax and social security relations, which will affect both the independent contractor and the other party to the contract.

Employment law

If a relationship is re-characterised as an employer-employee relationship, the independent contractor will be deemed to be an employee and will be entitled to claim a number of benefits, such as the right to be dismissed with notice (either through legislation, a collective bargaining agreement or a customary notice), dismissal with salary, pension contributions and other benefits under the relevant collective bargaining agreement, the payment of holiday pay, etc. The employee could also claim a legal severance payment in the case of unfair dismissal.

Non-compliance with the Danish Holiday Act will result in both the obligation to pay for holiday periods, which should have been supported by the employer and an obligation to pay salary or holiday allowances for future holiday periods. Furthermore, the employer will be liable for interest on holiday pay not paid to an employee and is likely to be fined for non-compliance.

Furthermore, if an employment relationship was subject to a collective bargaining agreement, but the agreement was disregarded by an employer, this will be considered a breach of the collective bargaining agreement, and will lead to a fine being imposed in accordance with Labour Court practice.

Tax law

The employer could be held liable for having withheld personal income tax, especially if the independent contractor cannot pay the income tax. Tax fines are likely to be imposed. However, the employer will not be solely liable for the taxes, because if the authorities request payment of the taxes from the employer, the latter will have recourse against the employee for the amounts paid. Furthermore, both the employer and the employee will be fined for tax evasion.

Supplementary Pension Scheme

In the event of a re-characterisation, the supplementary pension scheme will become applicable. In terms of this scheme, the employer is responsible for the declaration and payment of both the employee's and the employer's supplementary pension contributions in accordance with the Danish Act on Labour Market Supplementary Pension. The employer's contribution is a fixed monthly payment of approximately EUR 40 covering a fulltime employee; the employee's contribution is approximately EUR 20. Danish authorities may, in principle, impose a fine as a penalty for non-compliance with the scheme.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

A person seeking employee status may attempt to negotiate with his/her employer, but would normally have to file a lawsuit with the ordinary courts. If a trade union finds that an employer is in breach of a collective bargaining agreement, the Danish Labour Court will be asked to rule on this question.

Typically, it is only when the independent contractor relationship comes to an end and the individual concerned initiates legal proceedings, that the court will examine the employment status, as well as the contractual terms. When there are a sufficient number of elements, which are not compatible with the chosen form of employment status, it will be re-characterized as an employment contract and the individual concerned will,

based on their claim, be awarded several amounts depending on the execution and termination of their employment contract.

An alternative is to request the holiday authorities to assess whether the person is entitled to holiday pay or salary during holiday periods, which is an equivalent to seeking employee status through the courts. If the employer rejects the ruling from the holiday authorities, the employee will need to file a lawsuit against the employer.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

If the individual is considered an employee, he/she is likely to be entitled to compensation for any economic loss suffered, including for example salary and benefits during a notice period, severance pay and holiday pay accrued.

If the re-characterization is initiated by the tax authorities based on taxation issues, both the employer and the employee may expect to be liable for the payment of tax at source for the period of time when the independent contractor actually held the status of employee. Furthermore, the employee can expect an investigation into and a re-examination of his/her tax accounts for a number of previous years and tax-deductions made will be investigated in order to determine if they were made wrongfully.

Non-compliance with the Danish Holiday Act and with tax legislation is likely to lead to the imposition of fines and payments for interest related to mandatory payment of holiday pay and tax at source. Extensive tax evasion may qualify as a criminal offence and a breach of the Danish Criminal Code.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

A proper record of the relationship between an independent contractor and contractor will involve the drafting of a written agreement which reflects the nature of the relationship. This clearly worded agreement should reflect the general criteria provided by case law described above, including:

- representations by the contracting parties, including a representation by the independent contractor as a business partner with a specific VAT-number and as being responsible for the payment of taxes and VAT originating from the agreed work;
- a detailed description of the work and the result to be delivered, typically focusing on the result and not on the day-to-day work to be carried out by the independent contractor;
- estimated time of delivery and legal consequences if the agreed deadline is not met;
- when the payment of the purchase price becomes due; the purchase price should not become due until the work has been delivered, as a regular and continued payment or payment based on hours spent could potentially result in an interpretation that the work was in fact carried out by an employee;
- the contractor's responsibility to provide the working tools.

In other words, it should be structured in such a way as to include as many independent factors as possible, and avoid elements specific to a subordinate relationship. The written agreement is important in establishing the nature of the relationship.

b. Day-to-Day Management of the Relationship

In their day-to-day dealings with one another, the parties must ensure that the independent contractor is not a subordinate to the employer and that the management of their relationship is consistent with the contract. Accordingly, exercising close control over the work performed and giving detailed daily instructions must be avoided. Only general directives should be transmitted from the principal to the individual. The principal should give the independent contractor as much independence as possible.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

From a European perspective, the Danish labour market is considered attractive due to both a strong Danish economy and the specialised Danish labour market model, which benefits both employers and employees through flexible working conditions, employment terms and conditions based on individual or collective agreements and a high level of social security. In recent years, a number of independent contractors and businesses have been established in Denmark as a result; in particular specialists can benefit from establishing themselves as independent contractors, instead of working as employees. In recent years, a significant number of graduates from universities and business schools have shifted their career focus from being employed by well-known Danish and international businesses, to instead becoming owners of their own businesses, typically based in a start-up environment.

Another development is the appearance of so-called "atypical employees", a group of highly specialised individuals, e.g. journalists or IT specialists, who cater to a number of different employers or contractors as independent contractors, freelancers, consultants and employees depending on the work to be carried out or the character of the cooperation. Accordingly, an "atypical employee" might be both an employee and an independent contractor depending on how the specific relationship is structured. An "atypical employee" will benefit from a very flexible working method combined with the high level of social security mentioned earlier.

In recent years, unskilled work has moved away from Denmark to other countries due to the higher salary levels. In order to stay competitive, including avoiding high salary levels especially supported by collective bargaining agreements, certain employers involved in manufacture or who are dependent on an unskilled work-force (e.g. transportation by lorries and trucks), have redefined their employees as 'independent contractors' with the effect that the unskilled workers will not be protected by collective bargaining agreements, will not receive any pay during periods of sickness, will not receive holiday pay or be able to join a labour market pension scheme and will receive low rates of pay which are not in line with the labour market. Such bogus-employees have been brought to the attention of both Danish trade unions and the tax authorities.

b. Recent Amendments to the Law

In September 2014, the Danish High Court (High Court Western Division, 17 September 2014) ruled in a case regarding the employment of a Lebanese freelance interpreter, who assisted refugees with social work and interpretational work. The freelance interpreter was engaged by a company for a total of 24 months to perform interpretational work on a freelance basis. The interpreter carried out work on a regular basis; an employment contract was not entered into and the interpreter received his remuneration both as "salary" and as payments based on invoices issued by the interpreter to the company. As the interpreter was not guaranteed a specific number of hours of work, he was

entitled to reject work offered to him, he was free to organise the work in a way he preferred and as he had never challenged the fact that the company did not pay him holiday pay, the High Court ruled that the interpreter, despite the fact that he had on a number of occasions received a salary with the deduction of withholding tax, was not to be considered an employee of the company. Accordingly, the interpreter was not entitled to receive a salary during a notice period or a holiday allowance.

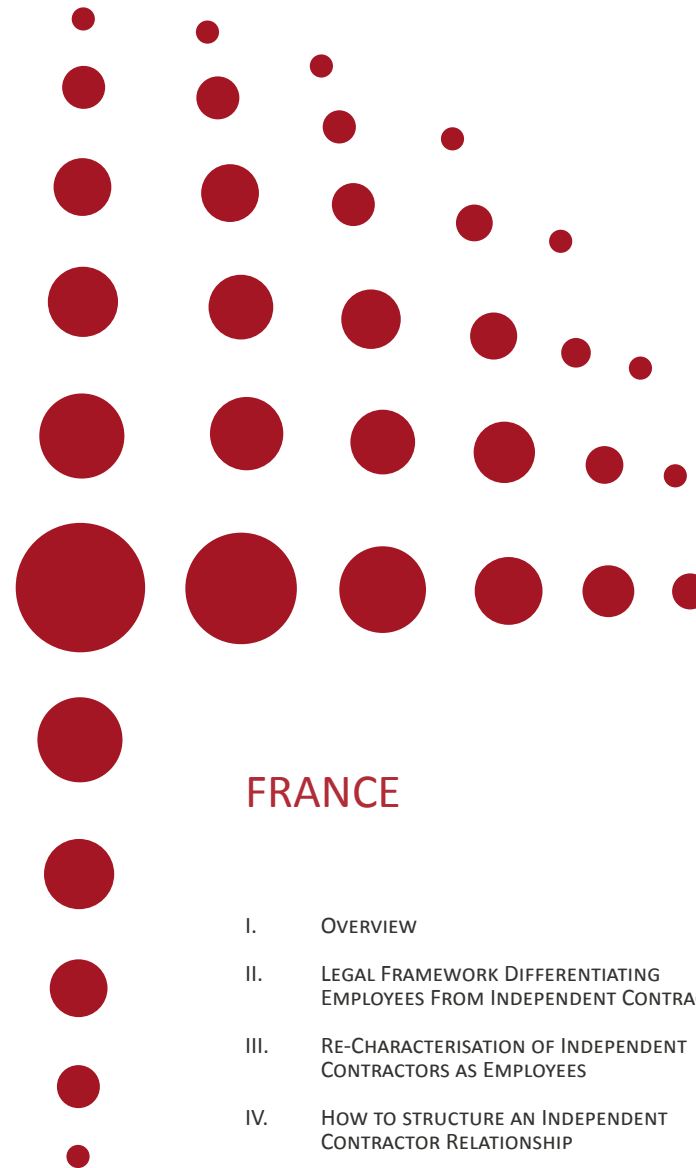
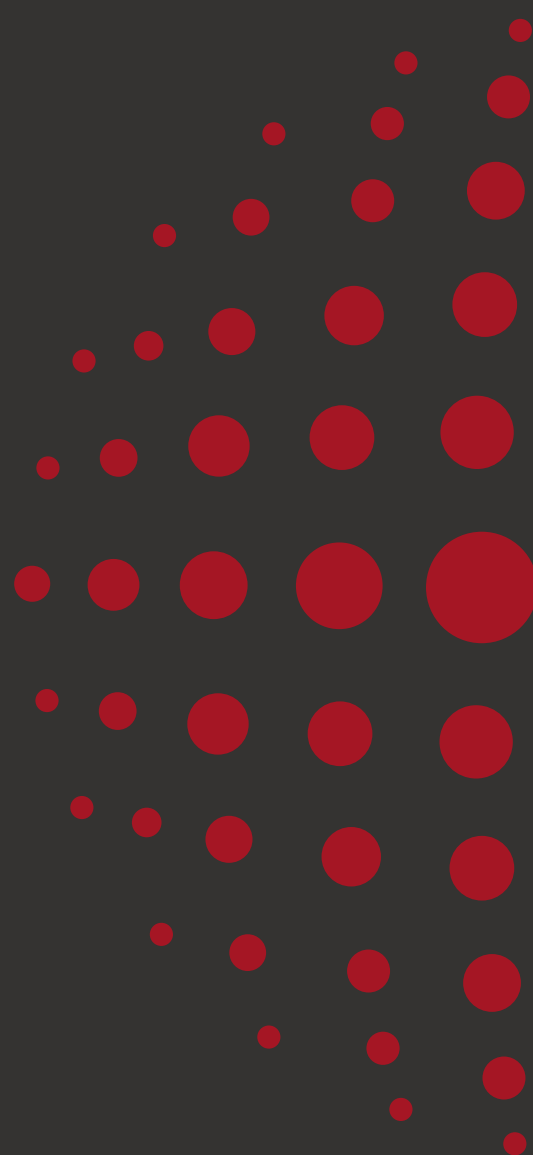
This ruling demonstrates that all aspects of the engagement must be considered carefully and individually before it is decided whether the relationship should be defined as an employment relationship or as an agreement with an independent contractor.

VI. CONCLUSION

The use of independent contractors in Denmark is increasing, and the primary reason for this development is because of how the Danish labour market is structured, where it is in the interests of both employers and employees for work to be organised as flexibly as possible.

The distinction between employees and independent contractors is defined by court rulings regarding employment protection, holiday pay and tax treatment. When distinguishing between an employee and an independent contractor the content of the contract is important. However, how the parties actually conducted themselves during their day-to-day relationship will prevail. Finally 'risk taking' is an important factor; an independent contractor bears the responsibility of financial risk in the work that he does, whereas an employee is only expected to provide his talent and time to his employer, but is not expected to bear any part of the financial risk of the business in which he is employed.

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FRANCE

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I. OVERVIEW

a. Introduction

The French labour code and its ten thousand laws apply to all employees in France, as do many social security laws. It can therefore be tempting to circumvent these obligations by preferring to do business using independent workers, who under French law are not considered employees and are therefore not subject to the same regulations and protections. The use of such contractual agreements in France has become increasingly popular over the past few years, allowing for what some consider to be greater flexibility, lighter costs, and less administrative bother. In reality, this practice is complex in its application and presents several limitations and risks that employers must be aware of. As we will see, not anybody can be an independent contractor, and in several scenarios, a judge may re-characterize the inappropriate services agreement as an employment contract. This judicial re-characterization of the relationship entails heavy legal, financial, administrative, and criminal consequences for the employer who wanted to avoid exactly such matters.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The notion of “employee” is not defined by French law. French case law defines it by defining the employment contract. An employment contract is defined as an agreement by which an individual works for another person (natural or legal), under the latter’s subordination, for which s/he receives remuneration.”

Therefore, three factors typify an employment contract: (1) discharge of tasks (2) remuneration and (3) relationship of subordination. As the first two factors are found in almost every agreement, a subordination relationship is the only factor, which allows to differentiate employees from other service providers, including independent contractors.

Article L.8221-6-1 of the French labour Code defines independent contractors as follows: *“is presumed to be an independent contractor, any individual whose working conditions are defined exclusively by himself or in a contract, in conjunction with his customer”*. The French labour Code also provides that individuals who are registered as self-employed service providers are presumed not to be linked to their customer with an employment contract in the execution of their activities. However, this is a refutable presumption, as the same article provides that the existence of an employment contract may however be established when the same registered individual provides services under conditions which place him in a permanent relationship of subordination with respect to his customer.

Therefore, the predominant factor, which differentiates employees from independent contractors, is **the subordination relationship**.

The French Supreme Court has ruled that a “subordination relationship is characterized by performance of duties under the authority of an employer who has the power to give orders, monitor execution of assigned duties and punish his subordinates’ breaches of duties” (Cass. Soc. 13 November 1996, n° 94-13187). Therefore, independent contractors should be “independent” when it comes to carrying out their duties. They carry out their work assignment autonomously, without receiving permanent instructions and/or orders from the company. Therefore, the key factors taken into account by the courts consist of **the frequency of the instructions, the monitoring of performance and possible sanctions**.

Other criteria, some of which are listed below, allow the courts to ascertain the existence of a subordination relationship. In their assessment, the courts use a set of factors. A single factor is not sufficient or decisive.

Working Hours: employees should comply with company working hours or time under penalty of disciplinary measures. On the contrary, independent contractors are not subject to company working hours, but have the latitude to arrange their working time as they wish.

Duties & Remuneration: employees have a permanent task for which they receive a regular monthly salary. Whereas, when a company calls upon an independent contractor, it is for his specific skills and a work assignment that the company cannot accomplish with its own staff. As for the remuneration, independent contractors are usually paid lump sum remunerations upon task accomplishment.

Place of Work & Work Equipment: employees usually work on company premises. The company should provide them with all necessary work equipment and materials. To the contrary, independent contractors should have their own work equipment. They could occasionally use company facilities but they mainly carry out their work by their own means. Independent contractors also have their own office, business card.

Exclusivity or Portfolio of clients: employees usually work for one employer while the independent contractor has a portfolio of clients.

Registration: employees are declared and registered with various institutions, notably the social security agency, by their employer who pays the relevant social security contributions on their behalf. To the contrary, independent contractors have to personally register as self-employed independent contractors and pay their own tax and social security contributions.

b. General Differences in Tax Treatment

Independent contractors are also subject to the income tax on their profits and can deduct their professional expenses from their professional income. They also have a different social security scheme. Independent contractors should pay their own contribution, which is slightly more costly than if they were employees. The main difference is that unlike employees, who are eligible for the Unemployment Fund which allows them to receive unemployment allowances paid by this fund in case of dismissal, independent contractors are not protected against this risk and do not contribute to this fund.

c. Differences in Benefit Entitlement

As for social security contributions, a company directly pays its own share and deducts the employee's share from his salary. As for benefit entitlements, a company has the obligation to affiliate its employees with relevant pension and healthcare institutions and pay its dues. Employees are subject to the income tax on their salaries.

d. Differences in Protection from Termination

French employment law is protective of employees. There is no concept of "employment at will" under French law, which means that any termination should be justified with valid grounds. In other words, termination of the employment contract is only possible if there is "serious and real cause" for termination. Termination of employment could be for personal reasons (e.g. poor performance, misconduct, etc.) or for economic reasons (e.g. redundancy as a result of the company's leading to the job's elimination or a significant change in the employment contract). The termination procedure is also

heavily regulated with obligatory timelines that must be followed. Once terminated (except in case of termination for serious/gross misconduct), the employee is entitled to a legal "severance package" which consists of dismissal indemnity, paid notice period and paid holidays indemnity. If the termination is on economic grounds, depending on the size of the redundancy plan, the employee also benefits from accompanying measures. Any unjustified termination would be deemed unfair, allowing the employee to sue the company and seek damages.

There are also specific protection periods for certain employees (e.g. pregnant employees, employees on occupational sick/accident leave, employees with a staff representative mandate). Termination of employment during the protection period is either impossible or only allowed under specific circumstances, under penalty of being null and void.

As for independent contractors, unlike employees, they do not benefit from any specific protection against termination, as it is not employment law, but rather commercial law, which applies to the services agreement. French case law stresses that termination of services agreements should not be abusive and the contractual notice period should be respected. Most services agreements are concluded for a definite period of time and contain a termination clause, which allows each party to terminate the services agreement, provided that a certain notice period is respected.

In a decision dated 22 January 2013, the French Supreme Court brought a certain level of protection to independent contractors. In this decision, the Court held that in case of non-compliance by the customer with the contractual notice period, the independent contractor is entitled to an indemnity amounting to the compensation he would have received until the term of the services contract. In this case, a services agreement for cleaning company premises was concluded for a period of one year, renewable tacitly. The services agreement provided that each party could terminate it by giving three months' notice before the renewal date of the agreement (i.e. by June 30th at the latest). The customer gave notice of termination by a letter dated July 4th (with 4 days of delay). The Court held that since the contractual termination notice was not fully respected, the customer had to pay to the independent contractor the sum of 216,463 euros, equivalent to one year of services.

e. Local Limitations on Use of Independent Contractors

Recourse to an independent contractor should be justified by the latter's specific know-how and skills, in order to carry out specific work that the company cannot accomplish with its own staff.

f. Leased or Seconded Employees

Companies could use different mechanisms to get a specific task done. However, in each case, the user company must remain vigilant not to put the employee in a subordination relationship so that a co-employment situation with the user company could not be claimed by the employee.

Temporary Work

Recourse to temporary employees ("*intérimaires*") is only possible to carry out a specific temporary task, called a "mission" and in cases exclusively specified by law (e.g. to replace an absent employee, temporary increase in business activity, seasonal work, etc.). The temporary employee is employed by the temporary work agency, which puts him at the user company's disposal for a specific period of time. The main advantage of this mechanism is that as the user company is not the direct employer, it does not have to deal with related employment issues with respect to the temporary employee. The temporary employee is paid directly by the temporary work agency, which then invoices

the user company for the rendered services.

Labour Leasing

The lending company puts its employee at another company's disposal to perform a specific task or mission. The lending company and the user company must sign an agreement which stipulates the duration of the labour leasing, the identity and qualifications of the employee, the method of determining wages, payroll taxes and professional fees invoiced by the lending company to the user company. Also, a rider to the "lended" employee's contract shall also be entered into, including some mandatory statements. Labour leasing is only valid if it is not lucrative. It shall be accordingly distinguished from subcontracting, an operation which does not only consist of posting employees (see below). The lending company can only invoice the user company for wages, social security fees and professional expenses incurred by the employee. Lucrative labour leasing is illegal, entailing heavy criminal and civil liabilities for the company. During the leasing period, the employment contract between the employee and the lending company is neither terminated nor suspended. The employee continues to belong to the staff of the lending company and remains paid by the latter. At the end of the labour leasing period, the employee regains his initial position within the lending company or if said position is no longer available, a similar position.

Subcontracting

The company calls upon a subcontractor to perform a clearly defined task that it cannot perform with its own staff, due to either economic or technical reasons. The subcontractor remains the sole employer of its staff. The subcontractor supervises and remunerates its staff and assumes all responsibility for carrying out the work assignment. The subcontractor is afforded a lump-sum remuneration for the accomplishment of the task, regardless of the number of working hours and employees involved. The subcontractor has its own work equipment, tools, facilities and clientele portfolio. This mechanism is very close to how independent contractors function.

g. Regulations of the Different Categories of Contracts

French employment law has regulated each category of employment contract (even though common roots could be found in some of them). Failure to comply with the legal requirements for each contract can result in civil and criminal liability for the company. Independent contractors are governed by civil or commercial law.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Courts are not bound by the denomination given by the parties to the relationship. According to the French Supreme Court *"the existence of an employment relationship does not depend on the parties' intention or the name they have given to their agreement, but on the actual conditions under which the work is performed"*.

This means that if the re-characterization factors are gathered, the court can re-characterize a services contract into an employment contract. The re-characterization of an independent contractor into an employee is not automatic and must be ordered by a court, which must first ascertain the existence of a subordination relationship between the independent contractor and his customer. The burden of proof lies upon the independent contractor who should demonstrate the existence of a subordination relationship.

b. The Legal Consequences of a Re-Characterisation

The re-characterization produces the following effects:

- the contractual relationship becomes an employment contract;
- the company or person using the services becomes the legal employer;
- the contractor becomes an employee.

Therefore, under this new legal status, the employer must apply the French Labor and Social Security Codes. As a consequence, the employer must:

- pay a minimum wage (SMIC or conventional minimum);
- paying charges and taxes on wages;
- apply the rules on hours of work including overtime;
- pay any sums related to a breach of employment contract.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

There are two ways for the request the re-characterization and declaration of an employment contract to come about.

It can occur following and administrative review or reassessment, or as a result of a claim directly from the worker who takes his action before the Labour courts (*Conseil de Prud'hommes*), requesting that his status as an employee to be recognized.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The re-characterization, should it be ordered, involves:

- Payment of overtime hours if any, bonus schemes and other benefits applicable within the company.
- Payment of social security contributions. Indeed, payments made to the independent contractor will be considered as "salary" and as such will be subject to employee/ employer social security contributions.
- Termination of the services agreement will be deemed as unfair termination entailing payment of the legal severance package (i.e. notice period, dismissal indemnity, paid holidays) and damages.
- The Criminal offence of "shadow employment" which may be constituted. The criminal offence of shadow employment (i.e. failure to declare salaried employment) is punishable by up to 3 years of imprisonment and a fine of up to €45,000 for the company's legal representative and a fine of up to €225,000 for the company as a legal entity. Moreover, a specific indemnity corresponding to at least six months' wages would be awarded against the company in case of termination of the relationship with the independent contractor, now considered as an employee. This is in addition to the other claims he may make regarding the re-characterization of the contract.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

The contract should avoid any terminology, description or reference to a remuneration-

mechanism that could be used in a re-characterization request by the worker (as described in part II). The definition of the mission and the terms must be very clear and allow for no ambiguity regarding the absence of a subordination relationship between the two parties. The autonomy granted to the worker must be explicitly stated in the agreement.

French case law has established that the calculation of the remuneration is a hint that the judge can use to determine that a contractual relationship must be re-characterized as an employment contract. In order to avoid this risk, the independent worker must receive a remuneration that is calculated based on the mission accomplished. In other words, it is essential to avoid calculating the remuneration based on the time the worker spends, as this may be used to request re-characterization.

During the relationship, it is important to ensure that the company requests the appropriate documentation regarding the independent worker's authorization to work.

The Company should not issue any pay slips. Normally, independent contractor's fees are not paid on a monthly basis, as it is the case for the employees. He is paid upon accomplishment of his work assignment.

b. Day-to-Day Management of the Relationship

As mentioned above, the existence of an employment relationship depends on the actual conditions under which the work is carried out, regardless of the name or terminology given to the relationship by the parties. As a result, in order to avoid any risk of re-characterization, it is imperative to make sure – on a daily basis – that the independent contractor retains his autonomy in carrying out his duties at all times. Below are a few guidelines on how to avoid such risk.

i. Make sure that the independent contractor is registered with the Trade Registry as a self-employed independent contractor. For services agreements with a value of at least 3,000 euros, the Company must verify that the independent contractor is in full compliance with his registration, social and tax requirements.

ii. Make sure that the independent contractor is not put under a subordination relationship. Therefore, he should not receive direct orders and instructions from the company. If the parties can establish tasks and objectives together, the independent contractor should remain as autonomous as possible when it comes to carrying out the work assignment.

iii. The independent contractor should not be given any company email, office, business card, or equipment. The latter could occasionally use company facilities, but it is necessary to make sure that he carries out his work mainly by his own means. He should have his own office outside the company. The company could allow him to occasionally use a company office, but he should not spend all his working time in the company office.

iv. Make sure that the independent contractor has his own portfolio of clients and that the company is not his sole client.

v. The independent contractor should not be subject to company working hours. He should be able to arrange his working time as freely as possible.

V. TRENDS AND SPECIFIC CASES

a. General Case Law tends to be Severe

Below are two important decisions from recent years which demonstrate how the courts assess various factors to determine whether or not a subordination relationship is established.

Cass. soc., decision dated 24 April 2013 n° 399

In this case, services agreements concluded with reality TV show participants were re-characterized into employment agreements. The judges, after looking into various factors establishing the existence of a subordination relationship held that *"there was between the Production team and the participants a subordination relationship characterized by the existence of an "agenda" which outlined the schedule for each day, imposed filming periods, repetition of scenes and repeated interviews conducted in a way that led the interviewee to say what was expected by the Production. The subordination relationship was also manifested in the Production's choice of clothing, imposed hours going up to 20 hours per day, obligation to live on the site and not to engage in personal activities, monetary penalties in case of departure during filming, and finally the obligation to follow activities organized by the Production which all put the participants in a dependency relationship with respect to the Production team (...)"*

Cass. soc., decision dated 10 April 2013 n° 11-27.384.

In this case the judges upheld the Court of Appeals decision and refused the re-characterization claim brought by a lawyer. The Supreme Court held *"given that MZ. had personal clients, was registered with the social security agency (URSSAF) as self-employed independent lawyer, his remuneration was paid either by his clients directly or as fees like other non-salaried lawyers, that specific materials were put at his disposal by the law firm to receive his own clients and finally on his headed paper he presented himself as a member of the law firm like other lawyers without mentioning his alleged salaried status (...) the Court of Appeal rightfully concluded from these factors that the subordination relationship was not established"*.

b. New and Expected Developments on the New Economic Actors

As in other countries, a recent hot topic is the arrival of new economic actors: companies such as Uber that are part of the new on-demand and sharing economy. The question pertaining to the qualification of their contracts and work agreements has been at the center of numerous cases recently and promises to change the legal landscape.

The French supreme court recently ruled that two drivers under an independent status employed by a taxi company could not obtain the re-characterization of their contracts as they did not demonstrate that they were at the company's permanent disposal, they were free to work with other companies, free to determine their schedule and that they had determined themselves the amount of their fee (Cass., soc, October 20, 2015, n°14-16178).

It also held that where drivers are in charge of their fees, their holidays, do not have to provide information on their mode of payment and are free to work for a number of companies, they are to be considered an independent worker and not an employee (Cass. Soc., March 17, 2016, n°12-29219).

The Paris Court of Appeals has also specified that the restrictions of geolocation, maintenance and tasks related to a vehicle imposed by the hire company were only linked to the necessity of ensuring the quickest and most efficient client service and did not, in itself, give rise to a relationship of subordination (CA Paris, January 7, 2016). In

these rulings, judges appear to focus on the means of carrying out the activity and the extent of liberty afforded to the driver to define this activity.

This is obviously a very new topic, but aware of the plethora of law suits pertaining to this matter, the French legislators have already taken action to clarify certain points regarding these new professional situations.

The recent Labour law of 2016 (commonly known as the “El-Khomri law”) introduced into French law the notion of independent workers using a platform, in particular those on the internet or through phone applications (for example, car-hiring/taxi services, food delivery services). The platform has a “social (or “employment”) responsibility towards the contractor, if it determines the characteristics of the service provided and sets its price. Furthermore, though the contractors are not covered by the same workplace insurance as employees, they may choose an insurance covering such risk, in which case the platform must cover the cost, up to a ceiling set out by a decree which has yet to be published. Moreover, this new law states that these independent contractors are entitled to professional training in the same manner that already exists for certain “liberal” or “independent” professions. The platform must cover the cost of this training. Lastly, the law creates collective rights for the independent contractors of a platform: in case of group action resembling a strike they are protected from sanctions and they can unionize.

2017 is a year rich in promised rulings and with the presidential and Parliament action, new legislation on the matter.

VI. BUSINESS PRESENCE ISSUES

a. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

From a tax law perspective, hiring one or more employees by a company with no place of business in France may raise some issues. As a principle, profits generated in France by a foreign company and distributed abroad are taxed in France. Therefore, the presence of an employee in France may be considered as a “permanent establishment”, subjecting the company to the payment of taxes in France.

b. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

Just as hiring one or more employees by a company with no place of business in France may raise issues, this would also be the case if the relationship with one or more independent contractors is re-characterized as an employment relationship. The same consequences will occur.

That being said, it should be noted that the notion of permanent establishment is defined by bilateral tax treaties. The European Court of Justice defines it as a structure with sufficient degree of permanence and capability in terms of staff and/or technical equipment, making it possible to render services autonomously (17 July 1997 ECJ case 190/195). Whereas, The French Conseil d’Etat defines it as a business installation with some stability - through which an activity generating profits is carried out – and with a certain degree of autonomy within the company.

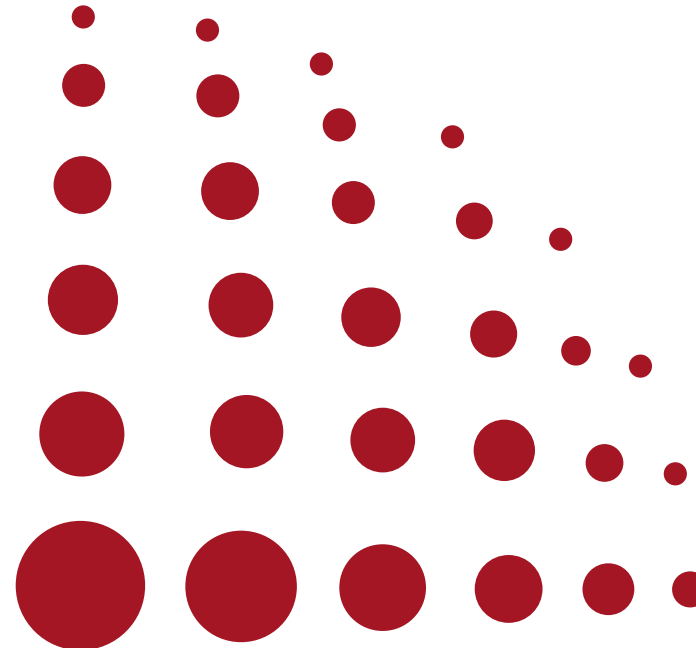
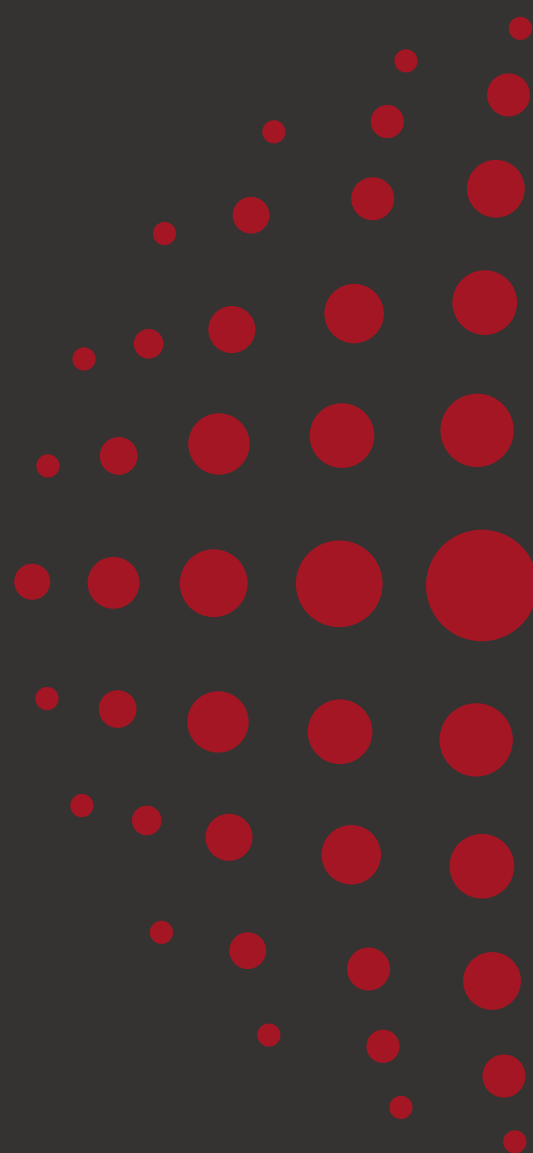
VII. CONCLUSION

Use of independent contractors brings more flexibility to the company; however, special attention should be given to the day-to-day management of such business relationships in order to avoid any risk of re-characterization and the serious consequences for the company that follow the re-characterization.

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GERMANY

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I. OVERVIEW

a. Introduction

The question, whether a person is an employee or an independent contractor by status may come up in various situations, e.g. during a company audit either of the contractor or the principal, during an investigation procedure by a prosecutor or by German authorities with respect to the payment of social security contributions, or – as will often be the case – in a dispute about the termination of a contract.

If employers err about the social status of their contractors, or deliberately try to avoid an employment relationship, several risks are involved. The employer will be held liable for paying social security contributions effectively for up to four years in arrears (in case of intent for up to thirty years), and employer's managers or directors may be subject to criminal prosecution for non-payment of these contributions. Furthermore, the pseudo-contractor may claim permanent employment with the employer.

Under German law, both the principal and the contractor, whose status is in doubt, may address the competent German authority and initiate a declaratory procedure about the contractor's social status. This procedure has the advantage of a clear and reliable assessment, whether a person must be regarded as an employee or can be treated as an independent contractor. However, in debatable cases the authority will often rule in favour of the status of an employee, where the status of an independent contractor may be very well justifiable.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

In Germany, the distinction between an employee and an independent contractor is not regulated by one specific regulation. There is a strict assessment under various criteria, which generate partly from German law regulations, but mostly from rulings of the German labor courts and the German administrative courts. Both courts use slightly different criteria for their assessment of whether a person is an employee or an independent contractor, which may lead to different rulings regarding their status. However, mostly, the assessment with both kinds of criteria will lead to the same results.

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

In Germany, the decision whether a person is an employee or an independent contractor, depends on numerous criteria.

German law indicates in the Commercial Code (*Handelsgesetzbuch – HGB*) that an independent contractor has the distinction of being able to freely determine his/her performance as well as his/her working time. In contrast, an employee is someone who may not determine his/her work performance free from instructions by the principal/ employer and is bound by specific working times.

However, as these criteria are rather vague, especially with regard to flextime wage accounts and highly specified jobs, and no other statutory regulation exists, the German Federal Labor Court (*Bundesarbeitsgericht*) specifies the distinction between a "dependent" employee and an independent contractor by the grade of personal dependence.

Therefore, the main criterion for the Federal Labor Court is whether a contractor is personally dependent on the principal. This will be assessed based on the scope of instructions, which the principal may give: If the principal may decide on the content of

the performance, the kind of performance, the time, duration and place of performance, and if the contractor is strictly bound by these instructions, then the contractor will most likely be regarded as an employee. Therefore, as a guideline it may be said:

The more the principal may determine the work performance of the contractor, the more likely the contractor is an employee.

Labor courts will therefore decide on the legal status of a contractor by an overall assessment of various criteria such as:

- how sophisticated are the working tasks given to the contractor (i.e. how to perform the assigned tasks)?
- how is the working time determined?
- how is the workplace determined?
- to what extent does the contractor's work depend on the principals' business organization (e.g. use of equipment and resources, team work with other employees)?
- in a valuing reflection, which of the two parties gains more directly from the performed services?

As these criteria are still vague and in border cases hard to assess, the social security authorities have developed several criteria, which may be taken into account when determining the status of an employee. These criteria are:

- does the contractor have to provide his services in person or may he engage an employee / subcontractor himself?
- who bears the economic risk of no performance or poor performance?
- is the contractor integrated into the business organization of the principal? • is the contractor named in duty rosters?
- who provides the equipment for the work performance?
- does the contractor have a regular workplace at the principal's location? Does he have an e-mail address or a telephone number? Is he registered in the principal's telephone book? Does he have branded business cards of the principal?
- does the contractor attend internal team meetings? Does he attend training sessions? Does he attend internal events like Christmas parties?
- is the contractor obliged to notify about holidays or other leave?
- does the contractor receive a fixed monthly remuneration or is he paid only for the services he actually provided?
- does he have to write invoices?
- is he covered for sick leave or for holiday?
- is there a fixed monthly payment?
- does the contractor have his own trade license / registered business?
- does the contractor announce / advertise his services in the market?
- does he work for other principals or is he at least free to choose other principals?
- how much payment does he receive overall by only one principal (more than 5/6 of his overall income)?
- how much time does he work for one principal?

The decision whether a contractor is to be qualified as an employee or an independent contractor, depends on an overall consideration of these criteria. In their considerations, labor courts tend to focus more on the degree of personal dependency, whereas the social security authorities rely more on the economic dependence of a contractor.

Finally, it should be noted that it is not relevant how the parties determine their contractual relationship. Especially, it is not relevant how the parties have designed their contractual relationship in the contractual documents, but how the contractual

relationship is exercised in the day-to-day business. Thus, even if both parties involved are convinced that their contractual relationship is a service agreement, it may still be assessed as an employment relationship by German courts or authorities and vice versa.

b. General Differences in Tax Treatment

The differentiation between an employee and an independent contractor has several consequences for the parties involved. Especially with regard to social security law and tax treatment, there are significant differences between an employee and an independent contractor.

Social security law

In Germany, a comprehensive statutory social security system is established. The system includes health insurance, long term care insurance, unemployment insurance and a state pension scheme. The system is funded by social security contributions of generally all workers that have the status of an employee. Both employer and employee pay these contributions, which are calculated on the basis of the employee's monthly gross salary. The employee's contributions are withheld from the salary and paid by the employer along with its own contributions as an aggregate amount.

In 2017, the contribution rates are as follows:

Health insurance	14.60 % (7.3 % employee; 7.3 % employer)
Long term care insurance	2.55 % (1.275 % employee; 1.275 % employer)
Unemployment insurance	3.0 % (1.5 % employee; 1.5 % employer)
Pension scheme	18.7 % (9.35 % employee; 9.35 % employer)

Exceptions are made for marginal employment, short term employment and student employees. Here, the social contributions may be paid as a lump sum and borne in their entirety by the employer or may not accrue at all.

As a general rule, independent contractors do not participate in the German statutory social security system. They need to arrange for their social security on their own accord, e.g. by means of private health insurance and private pension funds. Therefore, they usually receive a higher (gross) remuneration than comparable employees.

However, with regard to the statutory pension scheme and for specific professions, there are exceptions to this general rule. Independent contractors, who do not employ any employees themselves and are mainly engaged by one principal only, must participate in the German statutory pension scheme and make contributions to it. In contrast to employees, they must, however, bear the total contributions themselves.

Tax law

There are also differences between employees and independent contractors regarding tax treatment:

An employee's remuneration is subject to wage tax, which is a withholding tax and is deducted by the employer from the employee's monthly gross salary.

The services of an independent contractor are generally subject to VAT (*Umsatzsteuer*). Certain professions are excluded from the taxation, such as specific professional medical services. Furthermore, an independent contractor is exempt from such VAT taxation, as a petty trader, for annual revenue up to EUR 17,500, if the expected profit of the following year amounts, at most, to EUR 50,000. The independent contractor is responsible for transferring the incurred VAT and his personal income tax.

c. Differences in Benefit Entitlement

By virtue of statutory law, an employee is entitled to some particular benefits, each constituting a mandatory minimum level. Thus, employers may grant more, but never less than what is stipulated in statutory law. An independent contractor by contrast is not entitled to such benefits by virtue of statutory law. In fact, where a contractor is granted these particular benefits by his principal, this may imply a disguised employment. These particular benefits include:

Paid holiday leave

Employees must be granted at least 20 days of paid holiday leave, based on a five-day week. However, it is more common in Germany to grant employees 25 to 28 days of paid holiday. In addition, employees are entitled to receive their regular remuneration on statutory holidays (approx. 10 – 13 days per year), while they are generally not obliged to work.

Independent contractors on the other hand are, in general, not granted any paid holiday leave. This is only natural as independent contractors by definition do not have a specific working time and are therefore free to take days off at their own discretion. However, they are typically not granted any compensation for such time off, as they only get paid for services effectively rendered.

Paid sick leave

In case of incapacity to work due to illness, employees remain entitled to receive their remuneration from the employer for a term of up to six weeks pursuant to the German Act on Continued Remuneration (*Entgeltfortzahlungsgesetz – EFZG*). This covers both fixed remuneration as well as any variable remuneration such as bonuses. Under certain conditions, this entitlement applies several times per year, e.g. if the employee was healthy to work for a period of at least six months in between two instances of illness.

The German Act on Continued Remuneration does not cover independent contractors. However, with regard to § 616 German Civil Code (*Bürgerliches Gesetzbuch – BGB*) an independent contractor may claim compensation in case of incapacity to render his services for personal reasons, e.g. illness. However, this provision covers only a short period of time, generally less than a week, and its application may be excluded by the parties. As a general practice in Germany, independent contractors are not granted any compensation for sick leave at all.

Special allowances

Many employers in Germany grant additional benefits to their employees that are not mandatory, e.g. holiday allowance, Christmas allowance or surcharges for overtime work or work rendered on Sundays or statutory holidays.

Independent contractors, on the other hand, typically do not receive any such special allowances. Their remuneration usually exceeds the average salary of a comparable employee and no additional benefits are granted.

d. Differences in Protection from Termination

The difference regarding the termination of an independent contractor and an employee is extensive. Whereas an employee in general may only be terminated for a valid reason, an independent contractor may be terminated without cause, observing a contractual notice period.

Employees' protection against dismissal is divided into general and special protection. Special protection is provided to employees who generally face greater detriments in

case of a dismissal, such as handicapped or pregnant employees. In such cases, the permission of relevant government authorities is required prior to issuing a termination. Also, employees who act as employee representatives, such as a member of a works council or data privacy officers, enjoy special protection against dismissal.

As to the general protection, the freedom of the employer to dismiss an employee is substantially restricted by the German Act on Protection Against Unfair Dismissal (*Kündigungsschutzgesetz – KSchG*). The act applies if:

- a business establishment generally employs more than ten employees and
- if the employee has worked in the same company or business establishment for six months without interruption.

Under the Act on Protection Against Unfair Dismissal, a termination of employment by the employer is only legally effective if it is reasonably justified. Generally, a termination is only justified if it is based on grounds related to the person (e.g. impairments, lengthy or frequent illnesses) or the conduct (breach of contract) of the employee, or where compelling operational reasons, which preclude the continued employment of the employee in the business, exist.

Termination of an employee is generally subject to a notice period. Its term is governed by statutory law and ranges from two weeks to seven months on a sliding scale, contingent upon the duration of the employment relationship. The parties may agree to a prolonged term of the otherwise applicable statutory notice period.

In contrast, the contractual relationship with an independent contractor may generally be terminated for virtually any reason or no reason, except if the termination violates the principle of good faith. Parties may agree on specific reasons that need to be on hand to effectively terminate the contractor.

Termination of an independent contractor is generally subject to a notice period. In the absence of a provision in the contract, the term of the applicable notice period is based on the applied reference period for the payment of the agreed remuneration and varies between one day and six weeks to the end of a quarter. However, it is common to agree on a notice period of one month to the end of a calendar month in the contract.

Both employment relationships and relationships with independent contractors may, in case of severe breach of contract, be terminated for cause with immediate effect by the affected party.

e. Local Limitations on Use of Independent Contractors

There are no limitations on the use of independent contractors in Germany.

f. Other Ramifications of Classification

Other ramifications of the distinction between employees and independent contractors mainly relate to their scope of protection during the contractual relationship.

For example, most of the safety regulations, e.g. regarding the prevention of accidents at work, are only applicable to employees. Also, employers must abide by working time regulations for their employees, which do not apply to independent contractors.

Furthermore, employees enjoy limited liability regarding their work performance in case of normal negligence, while an independent contractor is generally fully liable in relation to his services.

Finally, the legitimate interests of employees are represented by a works council, who is not competent for the interests of independent contractors as they are not part of the workforce in its strict sense.

g. Leased or Seconded Employees

Under German law, it is possible to lease employees to another employer. In order to legally operate, the lessor (temporary employment agency) must hold an administrative permission, and the deployment of temporary agency workers must always comply with the requirements set forth in the German Act on Employee Leasing (*Arbeitnehmerüberlassungsgesetz – AÜG*) and other applicable law. Where a lessor does not hold said permission, any temporary agency worker deployed by him may claim full employment with the corresponding lessee.

As a general rule, the lessor is obligated to grant his employees (the temporary agency workers) the same fundamental conditions of employment that apply to comparable regular employees at the lessee's. This fundamental principle of German and EU legislation can be deviated from if the lessor applies a collective bargaining agreement for his employees. In the vast majority of cases, such collective bargaining agreements apply.

The main advantage of employee leasing is flexibility: temporary agency workers are not considered regular employees of the lessee/principal. As such they are not subject to dismissal protection, and therefore the principal can react quickly to a reduction of the work load and without further redundancy costs applicable in case of a restructuring process by cutting temporary agency workers. Vice versa, in case of an increased work load or in case specialized personnel are needed, employee leasing can be a useful option to increase the workforce without significant hiring costs.

Of late, costs have become more an issue than an advantage, as employee leasing is subject to a statutory minimum wage and the tariff-level is on the rise. Highly qualified temporary agency workers are usually more expensive than one's own regular employees anyway.

Strictly to be distinguished from employee leasing is the use of a contracting firm to fulfill certain services within the principal's business operation, e.g. facility management, cleaning services, operation of catering or canteen services, etc. The contracting firm will usually employ its own employees to perform the agreed services. When engaging a contracting firm, the principal must refrain from acting as the actual employer of the contracting firm's (i.e. external) employees. Otherwise, such use of a contracting firm may be considered as disguised employee leasing; its employees may then claim full employment with the principal. In order to assess whether a principal acts as the actual employer, the criteria to determine a contractor as an employee apply *mutatis mutandis*.

The distinction between employee leasing and use of a contracting firm is currently a very hot topic in Germany, and often principals are not aware of this issue. However, risks are major as imprudent principals may end up employing regular employees they never wanted on their payroll.

In April 2017, certain sections of the German Act on Employee Leasing will be amended. One of the main consequences of the amendment is the limitation on employee leasing: leased employees may only be employed by the same employer for 18 months. However, after a waiting period of three months, the employer is entitled to lease the employee again for another 18 months. This is likely to further affect the practice of employee leasing.

h. Regulations of the Different Categories of Contracts

Under German law, both contracts with independent contractors and contracts with employees are in substance service agreements. Therefore, both types of contracts do have the same roots and resemble each other. Both are subject to German civil law, mainly set forth in the German Civil Code.

However, as employees are historically regarded as more vulnerable, there are many special legal regulations that protect employees' rights and do not apply to independent contractors. Many of these protective regulations constitute a mandatory minimum and cannot be replaced by the parties to an employment contract. However, the terms and conditions of employment contracts, especially remuneration and benefits, are widely set and governed by collective bargaining agreements rather than by legal regulations.

As for independent contractors, there are scarcely binding rules regarding terms and conditions of their engagement.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As described above, the re-characterization as employee depends on several criteria, which have been developed by German federal courts based on the few scattered law provisions on this issue.

With regard to employee protection rights, the German labor courts usually decide on the legal status of a contractual relationship within the scope of a legal dispute over the application of a specific regulation or benefit that applies to employees only.

The social security authorities decide on the status of a contractor with respect to the question whether the principal/employer has complied with its legal obligation to pay social security contributions for every employee. For this purpose, the authorities audit employers regularly check for any unregistered employees, for whom social security contributions are due.

b. The Legal Consequences of a Re-Characterisation

The legal consequences of a re-characterization are broad and entail comprehensive risks for the employer.

In case of a re-characterization, the pseudo-contractor may claim employment with the principal/employer, thus gaining the status of an employee including the applicable level of protection. Specifically, the re-characterized employee may claim dismissal protection under the German Act on Protection Against Unfair Dismissal. This means that a termination requires a specific reason in order to be valid, and that the applicable notice period has to be observed. The employer may no longer terminate the contractual relationship without a valid reason.

Furthermore, the employer is, pursuant to German Social Code, obligated to retroactively pay social security contributions for the re-characterized employment relationship. In this regard, the employer is liable for the aggregate amount of the social security contributions without being allowed to deduct the employee's contribution from his/her salary in full. This obligation for payment of social security contribution arrears generally covers the entire duration of the re-characterized employment relationship and is thus only limited by the applicable statute of limitation. This means that the employer may

have to pay social security contributions for almost up to four years (in case of intent for up to thirty years) in arrears.

The employer's managing director/legal representative in charge may be held liable under criminal law for wrongful non-payment of the employee's social security contributions pursuant to the German Criminal Code. The legal representative may be sentenced to up to five years of imprisonment or charged with a fine, although this is rare in practice.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Persons seeking the status of an employee may address the competent labor court by lodging a declaratory action. If the claimant prevails, the court will declare that an employment relationship is in place and/or has been concluded at some particular point of time in the past between the claimant/employee and the defendant/employer.

As the employee status is *sine qua non* for some particular benefits or protective regulations to apply, a court will have to impliedly decide on a claimant's labor status if he/she sues the principal/employer for one of these particular benefits or protective measures. In practice, this commonly occurs following the termination of the contractual relationship by the principal/employer where the claimant would enjoy dismissal protection if qualified as an employee.

As previously mentioned above, principal and contractor may, either jointly or alone, also address the competent German authority and initiate a declaratory procedure about the contractor's social status. The authority's decision may be challenged by either party in court.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In the event of re-characterization, the employer must pay the outstanding social security contributions for up to almost four years (in case of intent for up to thirty years) in arrears, plus a late payment fine (generally one percent of the due amount per month).

Furthermore, penalties from a criminal conviction are possible and may include a sentence to imprisonment or a fine, whose amount depends on the income of the convicted employer/employer's legal representative. Any such penalties are imposed on the legal representative of the employer. The likeliness of such conviction is, of course, subject to an assessment on a case-by-case basis and rare in practice. Any form of criminal intent would necessarily be involved when misjudging the social status of an employee in order to justify a conviction.

If convicted, the employer/employer's legal representative may also be personally liable for the outstanding employee's social security contributions. This will particularly become relevant if the employing entity has filed for bankruptcy.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Under German law, it is not necessary to conclude a service agreement in written form. For purposes of evidence, however, it is recommended to agree upon a service agreement in writing.

Furthermore, all documents suitable as proof for the status as independent contractor

should be collected and maintained. This may include inter alia invoices, declarations/representations from the independent contractor, the contractor's business card, references on the contractor's marketing activities or employment with other principals, etc.

It is necessary to understand that the status of an independent contract cannot be determined or chosen by mutual agreement between contractor and principal. Instead, it is generally decisive how the contractual relationship is exercised in the day-to-day business. However, the service agreement with an independent contractor should still be properly drafted: it should include typical provisions of an independent contractor's contract and avoid any provisions that are indicative of an employment relationship.

b. Day-to-Day Management of the Relationship

When managing the contractual relationship with an independent contractor, it is highly important to observe the criteria detailed below. This means especially, that the independent contractor should **not** receive:

- i. Instructions on when to work
 - Better: Give a time line, when the project must be finished.
- ii. Instructions on how to work
 - Better: Give instructions on what characteristics the final work product shall have.
- iii. Provide equipment
 - Better: Let the independent contractor work with his own equipment.
- iv. Provide a regular work place, telephone line, e-mail address
 - Better: Let the independent contractor work at home or at a flexible work place in the office.
- v. Fixed payment every month
 - Better: Payment per day/hour actually worked in a month, or a lump sum payment upon the achievement of milestones of the work product.

By such management of the contractual relationship, it is possible to demonstrate that the independent contractor is not integrated into the principal's business organization. The allegation of an employment relationship can thus be disproved.

V. TRENDS AND SPECIFIC CASES

a. Recent Amendments to the Law

In April 2017, a new provision of the German Civil Code (§ 611a BGB) will enter into force, which defines the conditions of employment contracts. This will be the first time that such a legal definition exists in the German Civil Code. The new regulation is intended to bring about more legal security. Nevertheless, a big change is not expected due to the fact that the new section includes most of the courts' criteria for the assessment of whether a person is an employee or an independent contractor.

Furthermore, in April 2017 new regulations of contracts for employee leasing will come into force. Pursuant to the new regulations, lessors and lessees are obliged to characterize employee leasing explicitly as "employee leasing". Currently, the lessor and the lessee often characterize agreements about employee leasing as service or project contracts in order to avoid the protective regulations of the German Labour Law. If it turns out that

the agreement must be characterized as employee leasing, the parties could avoid legal consequences if the lessor held a precautionary permission of employee leasing. From April 2017 onwards such a precautionary permission will no longer be allowed.

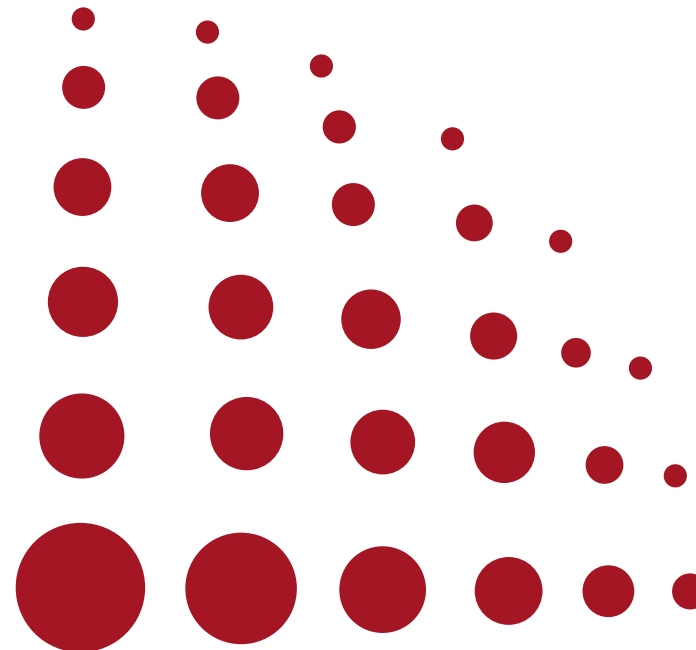
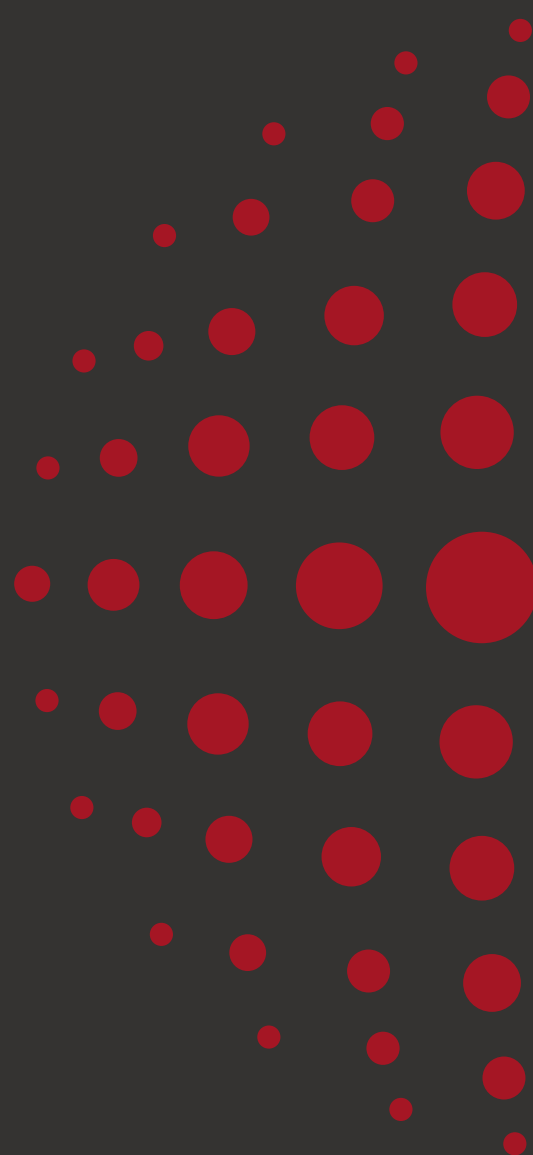
VI. CONCLUSION

Under German law, the entrepreneur is generally free to decide whether certain tasks within its business operation shall be fulfilled by its own (employees) or an external workforce (independent contractors). From a purely legal perspective, this decision should mainly be influenced by the nature of the work or project in question, as the main criteria when determining the legal status of the engaged worker refer to the place, time and exact manner of the work to be performed as well as a necessary integration into the principal's business organization. However, a feasible solution in practice has to factor in more than just legal aspects. When making this decision, the entrepreneur should in any case be very much aware of the risk of a disguised employment, i.e. the possible consequences of a situation where a supposed independent contractor will be qualified as an employee. In many cases such risk can be significantly mitigated if the relationship with the independent contractor is prudently structured and managed.

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HONG KONG

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I. OVERVIEW

a. Introduction

In Hong Kong, the Employment Ordinance (“EO”) is only applicable to employers and their employees that are engaged under employment contracts. In other words, only employers and employees are entitled to rights and benefits under the EO and not persons that are engaged as independent contractors. Consequentially, care must be taken to ensure that any staffing arrangement’s legal implications are consistent with those that are intended by the parties to prevent disputes. This article provides an outline of the employment law in Hong Kong, and the associated consequences in the event of a re-characterization of relationship. It will identify the factors that are likely to indicate the existence of an employment relationship, and will discuss the appropriate method of structuring independent contracting arrangements.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Unfortunately, there are no hard and fast rules in differentiating whether an individual is an employee or an independent contractor under Hong Kong law. The Hong Kong Court will look critically at the factual matrix and all relative factors to determine the true relationship in substance, regardless of the label given to the parties’ agreement. In other words, a well-drafted and properly executed contract and the terms therein may not be determinative of the parties’ relationship. For example, even if a business hires a worker as an independent contractor, the Court may still find that there is in substance an employment relationship in which the business will be required to meet all the obligations under the EO to the contractor as if he was an employee of the business. As such, it is important to delineate between the status of an employee and an independent contractor when parties enter into a service agreement to avoid potential disputes and infringement of the law.

The starting point is for the Court to ask whether the person who has been engaged to perform the services is performing them as a person in business on his own account.¹ If he is performing these services on his own account then the contract is more likely to be a contract with an independent contractor. On the other hand, if he is not performing these services on his own account but on the employer’s account, the contract is more likely to be an employment contract. This is a question of fact and the worker has the burden of proof that he is an employee on a balance of probabilities.²

Historically, different tests used by the Court include:

- the intention of the parties of their relationship;
- the degree of control the worker has over the job; and
- the structure and the arrangements; and so on.

The recent approach is that the Court will take an overall impression approach. It will examine all relevant factors including ones identified in the case law (which includes the intention test and control test as stated above) and any other relevant factors.³

¹ Lee Ting Sang v Chung Chi Keung [1990] 1 HKLR 764;

² Yeung Tin Sang v The Brothers Co [2001] HKEC 1493;

³ Wong Kin v Him Kee Food Distribution Co Ltd [2016] 2 HKLRD 665;

The list of relevant factors is not exhaustive. Further, it is difficult to tell as to how important a particular factor should be or how much weight the considerations should carry in a particular case. All details are not of equal weight or importance in any given situation and the details may also vary in importance from one situation to another.⁴

Despite the fact that the Court takes an overall impression approach and will take all relevant factors of each specific case into consideration, there are factors which the Court has often found to be of relevance in making the determination, bearing in mind that the weight to be given to each will vary depending on the circumstances of a particular case.

Express terms of the written contract

As mentioned above, an express term in an agreement stating that the worker is an independent contractor would not be determinative of the worker's status. The express terms would be only one of the many factors in which the Court would consider and such terms would only be of minor influence.⁵ It is when the Court, in considering all the relevant circumstances, finds it doubtful as to the rights and duties the parties wished to provide for, that the written terms would be useful.⁶

Degree of control and level of supervision

Control used to be a sufficient indicator of an employment status. Although it is no longer a sufficient indicator of an employment status, it nonetheless remains the most important consideration in many cases.

A high degree of control by the employer over the worker such as control as to what, when, where and how the work is to be done would often give weight towards a finding of an employer-employee relationship. Examples of control are (i) prohibition against working for others; (ii) regular hours of work; (iii) close supervision; (iv) provision of transportation between work sites;⁷ (v) choice of co-workers; (vi) specific instructions as to when and where to work;⁸ (vii) requirement to wear uniforms;⁹ or (viii) requirement to seek permission before taking leave.¹⁰ On the other hand, if the degree of control from the employer is limited, such as the ability to reject the work, weight will be given towards the finding of a business-independent contractor relationship.

The kind of work involved can have some weight towards whether the relationship is one of employer-employee or business-independent contractor. For example, jobs such as laborers, which by nature generally involve a high degree of monitoring and control would usually be weighted towards an employer-employee relationship. On the other hand, although not determinative, jobs such as advisors or portrait artists which by nature generally involve very limited degree of monitoring and control would usually be weighted towards a business-independent contractor relationship.¹¹

Work Delegation

Where the worker is allowed to freely delegate work to another or hire other workers for the job, this will be weighed towards there being a business-independent contractor relationship. In other words, any restrictions regarding work delegation or hiring of other workers to assist will often support the finding of an employer-employee relationship.

This factor does not appear very often in case law but when it does, although not a

decisive factor, it carries considerable weight.¹² This is because the freedom to be able to hire other workers itself is inconsistent with the idea of the employer having control.

Equipment and Machinery

An employer providing machinery and equipment (including safety equipment) necessary for the job for a worker will be weighted towards the finding of an employer-employee relationship. Although not determinative, this factor is often mentioned in case law in a finding of an employer-employee relationship.¹³ There are also cases where the Court would consider the fact that certain workers such as artisans, drivers and other skilled workers would be expected to have their own tools and equipment by nature of their job.¹⁴

Financial Risk

A worker being exposed to financial and profit risks would generally be weighted towards there being a business-independent contractor relationship. It is important to note that financial risk here does not include (i) a worker's ability or chance to increase his salary by gaining more experiences and working harder or to decrease his salary;¹⁵ or (ii) a management worker having some discretion as to his salary and bonus. Rather, financial and profit risk here refers to a worker putting his own financial resources or other resources at risk in his business with the chance of gaining or losing.

Positive actions of the employer and employee

Although not determinative, the Court will consider certain positive actions of the employer or employee. One example is the payment of Mandatory Provident Fund ("MPF") payments. Pursuant to the Mandatory Provident Fund Schemes Ordinance¹⁶, employers in Hong Kong are required to make contributions to the MPF for all their employees. The Court has in some cases treated an employer not paying MPF contributions for his worker as a factor weighing towards the worker being an independent contractor.¹⁷ However, the Court generally does accept that the employer can easily withhold from making MPF contributions to argue against the existence of an employer-employee relationship and hence, in general, this factor is not determinative.

On the other hand, if MPF contributions are solely made by the worker himself as a self-employed person, it will be a factor weighted towards there being an independent contractor relationship and more weight would generally be given, in comparison to the abovementioned scenario where no MPF contributions were made by the employer.¹⁸ Similarly, this is not conclusive and is only one factor which the Court would consider.

Another example is income tax filing. Employers are generally required to file tax forms for their employees and the filing of salaries tax returns by employers for their employees was found to be an important factor weighing towards there being an employer-employee relationship.¹⁹

b. General Differences in Tax Treatment

An independent contractor whose profit comes from the provision of services or purchase and sale of goods is usually considered a self-employed person for tax purposes in Hong Kong. As a self-employed person, he is subject to profits tax based on the profits of his business or his partnership's business.

⁴ Poon Chau Nam v Yim Siu Cheung [2007] 1 HKLRD 951;

⁵ Chan Siu Ming v Kwok Chung Motor Car Ltd [2008] HKCLR 13;

⁶ Yeung Tin Sum v Wong See Ting [2007] HKEC 694;

⁷ Leung Chun Pong v Cheng Man Tung [2008] HKEC 1001;

⁸ Yeung Tin Sum v Wong See Ting [2007] HKEC 694;

⁹ Wong Wai Ming v FTE Logis,cs Interna,onal Ltd [2008] HKEC 1441;

¹⁰ Wong Wai Ming v FTE Logis,cs Interna,onal Ltd [2008] HKEC 1441; Job nature

¹¹ Rick Glofcheski and Farzana Aslam (2010) Employment Law and Practice in Hong Kong, Sweet & Maxwell;

¹² Nguyen Van Vinh v Cheung Ying Construction Engineering Ltd [2008] HKEC 882;

¹³ Cheung Wai Yick v Lau Kin Wing [2009] HKEC 268;

¹⁴ Chan Suet Hung v Lan Field Marble Co Ltd [2003] HKEC 1498);

¹⁵ Chan Siu Ming v Kwok Chung Motor Car Ltd [2008] HKCLR 13;

¹⁶ Mandatory Provident Fund Schemes Ordinance (Cap 426)

¹⁷ Helskens Jan Bert Julia v AXA Interna,onal Ltd [2008] HKEC 1450;

¹⁸ Poon Chau Nam v Yim Siu Cheung [2007] 1 HKLRD 951;

¹⁹ Chan Sau Ying v Yuk Lung Sauna [1995] HKLY 575;

The exact computation of salaries tax in Hong Kong is outside the scope of this article but to give a taste of what it is like and to compare that with an employee below, generally speaking the current profits tax rate in Hong Kong is 16.5% of the assessable profits for corporations and 15% for unincorporated businesses, irrespective of their residential status and subject to certain reliefs and deductions as stated in the Inland Revenue Ordinance²⁰ or other relevant rules and laws of Hong Kong. In this regard, a self-employed person is required to:

- prepare accounts and any relevant reports based on the accounting records;
- prepare and file a tax return to report the profits or losses of the business;
- inform the Inland Revenue Department (“IRD”) regarding his tax liability within 4 months from the end of the basis period for the relevant assessment year, except where he received the relevant tax return of the IRD;
- pay the tax as required;
- maintain the business records for at least 7 years;
- if his business has ceased, inform the IRD within 1 month of the cessation; and
- if there is a change of address, inform the IRD within 1 month of such change.

On the other hand, an employee has to pay salaries tax on his taxable income derived from Hong Kong from any employment. Hong Kong salaries tax is calculated based on the chargeable income at progressive rates.

c. Differences in Benefit Entitlement

EO is the primary piece of legislation governing employment conditions in Hong Kong. EO is generally applicable to employers and employees that are engaged under employment contracts. Some examples of benefits include rest days, wage protection, paid statutory holidays, paid annual leave, paid maternity and paternity leave, severance payment, long service payment, protection against unreasonable and/or unlawful dismissal and so on.

The Employees’ Compensation Ordinance (Cap. 282) (“ECO”) is another piece of important legislation, which is applicable to all employees employed under an employment contract of service or apprenticeship. It sets out the entitlements of employees who are injured by accidents or who suffer from specified occupational diseases arising out of and in the course of their employment. ECO also requires an employer to take out proper employee insurance policies.

There is other legislation that governs the interests and obligations of the employers and employees. One example is the Minimum Wage Ordinance (Cap. 608) (“MWO”), which sets out a minimum wage requirement for employees. The Mandatory Provident Fund Schemes Ordinance (Cap. 465) (“MPFSO”) operates like a compulsory pension scheme which requires every employer to take all practicable steps to ensure its employees are members of a registered provident fund schemes, and requires both the employers and employees to contribute to the provident fund schemes set up in favour of the employees.

In other words, in addition to the employment contracts entered into by employers and employees, their respective interests and obligations are also protected and governed by statutory legislation. On the contrary, the respective interests and obligations for a business-independent contractor relationship are merely set out in their respective service agreements.

d. Differences in Protection from Termination

For employment contracts, generally speaking, except in special circumstances, either

²⁰ Inland Revenue Ordinance (Cap. 112);

party to a contract of employment may at any time terminate the contract either orally or in writing, by giving the other party sufficient notice of his intention to do so. Pursuant to EO, the statutory length of notice required to terminate a contract of employment (except during expressed probationary periods) shall be as follows:

- for a contract for one month renewable month to month which does not make provision for the length of notice required to terminate the contract – not less than one month;
- for a contract for one month renewable month to month which makes provision for the length of notice required – the agreed period but not less than 7 days; and
- in every other case, the agreed period but not less than 7 days.

In addition, either party could also terminate the employment immediately by paying the other party a sum calculated by multiplying the number of days / months required as the notice period by the daily / monthly average of the wages earned by the employee during (i) the period of 12 months immediately before the date on which the party terminating the contract gives notice of the termination to the other party; or (ii) if the employee has been employed by the employer concerned for a period shorter than 12 months immediately before such date of notification, the shorter period. In contrast, without the protection of EO, an independent contractor’s relationship with a business is merely contractual in nature. Any termination of the contract shall be governed by the actual contractual terms (which may be expressed or implied).

e. Local Limitations on Use of Independent Contractors

Whilst workers in Hong Kong are generally free to enter into service agreements of any nature, there are certain professions, which are regulated by statute, industry rules and codes and where the use of independent contractors is restricted, for example judicial officers and pupils to barristers-at-law.

Having said that, the use of independent contractors in Hong Kong has become increasingly common. There is also a lifestyle trend where, instead of being confined by fixed working hours, people prefer to work from home independently, spend more time with their families, and to develop their own businesses.

In the meantime, Legislative Council Members and trade unionists have expressed concerns on the number of workers being labeled as self-employed persons notwithstanding that they have all the indicia of an employee (as discussed above).²¹

However, as mentioned, in Hong Kong, if in substance the relationship as stated in the contract is in fact one of an employer-employee relationship, how the relationship is labeled is immaterial.

Further, an employer cannot unilaterally modify an employee’s classification to an independent contractor. If the employer does unilaterally make such modification, a claim may be filed against the employer on the basis of variation of the employment contract unreasonably under EO. Alternatively, the employee might be able to claim against the employer for termination compensation on the basis of constructive dismissal.²²

f. Other Ramifications of Classification

Insolvency Ramifications

When an employer becomes insolvent, its employees may file a winding-up or bankruptcy

²¹ Legislative Council Panel on Manpower, Employees vis-à-vis Self-employed Persons (19 November 2009) LC Paper No. CB(2)276/09-10(03);

²² *ibid.*;

petition to recover the debts owed by the employer which includes arrears of wages, wages in lieu of notice, severance payment, untaken annual leave and statutory holidays and so on. Similarly, independent contractors may also file a winding-up or bankruptcy petition to recover the debts owed by the business or individual.

The Protection of Wages on Insolvency Ordinance (Cap. 380) (“PWIO”) protects employees during the winding-up of a corporation or bankruptcy of an individual employer in the sense that the aggrieved employees can apply for ex gratia payment under the PWIO for the outstanding wages, wages in lieu of notice, severance payment, untaken annual leave and statutory holidays and so on. It should be noted that such protection is not available for independent contractors.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Re-characterization may happen when a worker who was stated as an independent contractor on the service contract, alleges that he is entitled to employee’s compensation under ECO and argues that he is an employee in substance instead of an independent contractor.

The leading authority in Hong Kong on the issue of whether a person is an employee of another is *Poon Chau Nam v Yim Siu Cheung*²³. As discussed above, it laid down the rule that the modern approach to the question of whether a person was an employee was to examine all the features of the parties’ relationship against the background of the indicia of employment, with a view to deciding whether, as a matter of overall impression, the relationship was one of employment.

The modern approach involves a “nuanced and not a mechanical approach”, and is not an exercise of running through items on a check list to see whether they are present in, or absent from the situation. Its object is to paint a picture from the accumulation of details, whereby not all details are of equal weight or importance in any given situation and the details may also vary in importance from one situation to another. In undertaking the modern approach, the indicia includes the degree of control exercised by the employer; whether the person performing the services provided his own equipment; whether he hired his own helpers; what degree of financial risk he took; what degree of responsibility for investment and management he had; and whether and how far he had an opportunity of profiting from sound management in the performance of his task. As such, the Court will not necessarily endorse whatever labels the parties choose to put on their relationship.

In *Wong Kin v Him Kee Food Distribution Co Ltd*²⁴, a recent case where the Court had to determine the status of the applicant, thereby entitling him to claim employees’ compensation under ECO for injuries sustained during the course of his employment, citing *Chan Kwok Kin v Mok Kwan Hing*²⁵ and *Ferguson v John Dawson & Partners (Contracts) Ltd*²⁶, the Court stated that the parties’ classification of their relationship is not conclusive and it is for the Court to evaluate the facts and determine the legal relationship.

It is important to note that the abovementioned indicia are again not exhaustive. As applied in *Lee Ting Sang v Chung Chi Keung & Another*²⁷, no exhaustive list has been

²³ [2007] 1 HKLRD 951;

²⁴ [2016] 2 HKLRD 665;

²⁵ [1991] 1 HKLR 631;

²⁶ [1976] 1 WLF 1213;

²⁷ [1990] 2 WLR 1173 at para 382;

compiled and perhaps no exhaustive list can be compiled of the considerations which are relevant, nor can strict rules be laid down as to the relevant weight which the various considerations should carry in particular cases²⁸.

b. The Legal Consequences of a Re-Characterisation

Even if the person is called or has been labeled as an independent contractor in the contract, if in essence an employer-employee relationship exists, the employer will be required to fulfill its responsibilities under the relevant legislation by paying back statutory benefits retroactively to the worker who has been falsely labeled as an independent contractor.

As mentioned above, such rights and benefits include basic protection under EO such as paid annual leave, paid maternity and paternity leave, statutory holiday pay, sickness allowance, severance payment or long service payment, minimum notice of termination and right to make a payment in lieu of notice, etc.; the statutory Minimum Wage under MWO; statutory sick leave and compensation arising from work injuries under ECO; and employer’s MPF contributions under MPFSO.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

Whether a person is or is not an employee is a question of fact, which is essentially a matter for the Labour Tribunal or the Courts of Hong Kong to determine. Apart from judicial remedies, a complaint hotline is in place to facilitate the reporting of non-compliant employers by employees who suspect that they have been deprived of statutory rights and benefits. As with the modern approach, the Labour Department will conduct investigation by examining the substance rather than the form of the relationship, and will prosecute the employer if it is found that the employer has breached the relevant statutory rules. The Labour Department has the general power to prosecute non-compliant employers.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

In Hong Kong, cases have shown that whether a person is acting in his or her capacity as an employee or an independent contractor is often a mixed question of fact and law. Therefore, such a distinction of the two relationships will not merely rest upon a written document, but also upon all factual circumstances of a particular case.

Notwithstanding such, if both parties intend to have an independent contractor relationship, they are strongly recommended to incorporate clear and express provisions into the independent contractor agreement to reflect such intention, and to put the matter beyond doubt as much as possible. Express provisions that reflect independent contractor factors can play a significant role in indicating the nature of the relationship between the parties. Among all express provisions, the most important provision will state clearly that the person is engaged as an independent contractor and not an employee or subsidiary of the principal. Other examples of these independent contractor factors include:

- contractor’s right to hire his or her own workers and delegate work to them;
- contractor’s right to control over how the work is to be carried out, for example by using his or her own work tools in completing the work;

²⁸ *Market Investigations v Minister of Social Security* [1969] 2QB 173 per Cooke J at para184;

- contractor's right to select the site at which work is performed;
- contractor's right to procure services from other potential clients;
- contractor's right to fix his or her own time schedules as opposed to following a strict schedule prepared by the principal;
- contractor should take up liabilities for all of the debts, losses, and expenses on his or her income solely; and
- payments to the contractor should be result-based and not just based on hours spent on working.

In addition, the principal must avoid setting out conditions that imply subordination, such as assigning a supervisor to give contractor directions on how the work is to be carried out. The independent contractor should also undertake not to allege that he or she is the employee of the principal during and even subsequent to the termination of the independent contractor agreement.

b. Day-to-Day Management of the Relationship

Parties are advised to seek and obtain independent legal advice in the course of negotiating the independent contract agreement. All discussions should be documented by the parties to ensure that the clear intentions of the parties, at the time of the agreement, is delineated in the agreement. The significance of a properly defined and documented independent contractor relationship should not be overlooked as it sets out a clear and enforceable mutual understanding of the rights and obligations of the parties.

On top of safeguarding the rights of the parties whilst concluding the agreement, the principal should make every effort to preserve the level of independence granted to the independent contractor. These include the rights provided in the independent contractor agreement as stated above. Any interference of these rights by the principal might be a factor hinting an employer-employee relationship instead of a business-independent contractor relationship. As such, principals are recommended to draw up written evaluations on a routine basis concerning the independent contractor's scope of work. Such evaluations may be useful in refuting any future claim of re-characterization.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The recent case of *Wong Kin v Him Kee Food Distribution Co Ltd*²⁹ reaffirms the idea that the Court would look at all the relevant factors overall in determining the relationship between contracting parties and Independent Contractors.

In the said Judgement, the Court reaffirms that there is no single test that can conclusively point to the distinction between an employee and an independent contractor. The approach taken by the Court is to examine all features of the parties' relationship against the background, and the Court will then decide, as a matter of overall impression, whether the relationship is one of employment.

b. Recent Amendments to the Law

The Contracts (Rights of Third Parties) Ordinance (Cap. 623) ("CRTPO") came into force on January 1, 2016. Before the enactment of the CRTPO, only parties to a contract (such as a company and its customer in a sale of goods contract) should have the rights to

enforce the contract terms. Even if a contract confers certain rights and benefits on a third party, the contract cannot be enforced either by or against such third party. With CRTPO coming into force, subject to certain requirements below, independent contractors may be able to enforce their rights as third parties in a range of business-related contracts.

CRTPO does not apply to all types of contracts. It only applies to contracts entered into on or after the commencement of CRTPO. Existing contracts will not be affected. The following types of contract are explicitly excluded from the operation of CRTPO³⁰:

- bills of exchange;
- promissory notes;
- negotiable instruments;
- deeds of mutual covenant;
- any covenant in relation to land;
- contracts of carriage;
- lenders of credit;
- a company's articles of association; and
- a term of contract of employment against an employee.

Under the CRTPO, third party rights will only be conferred if the contract expressly provides that the third party may enforce a term of contract, or if the contract contains a term that purports to confer a benefit on the third party. In addition, the third party must be expressly identified in the contract by name, as a member of a class or by as answering a particular description³¹. If these conditions are satisfied, the third party would be entitled to any remedy that would have been available to him in an action for breach of contract if he had been a party to the contract³².

For example, if there is a contract between a company and the company's customer and the contract anticipates the engaging of an independent contractor to perform work for the company, where the independent contractor is expressly identified, CRTPO would allow the independent contractor, although being a third party to the contract, to claim his rights against the customer. Section 4 of CRTPO also provides an option, whereby contracting parties do not wish to enable third party enforcement, to make a clear express provision to that effect in the contract. In that case, the third party or independent contractor in our example above will no longer be able to rely on CRTPO to claim his rights under the contract (if he was not made a contracting party).

VI. CONCLUSION

The foregoing summarises some of the major distinctions between employees and independent contractors under Hong Kong law.

In determining whether the person in question is an independent contractor or an employee, the Court will adopt the modern approach and examine all the features of the parties' relationship against the background of the indicia of engagement.

The parties' labeling of their relationship is not determinative, nor would it be considered the sole factor, which the Court takes into account. Hence, on top of stating the nature of the service relationship, it is important for parties to clearly define any employment/contract of services relationship and delineate the scope of work and each party's responsibilities and obligations from the outset, in order to ensure that the terms reflect the parties' common intentions and that the terms are consistent with the service

²⁹ *Wong Kin v Him Kee Food Distribution Co Ltd* [2016] 2 HKLRD 665;

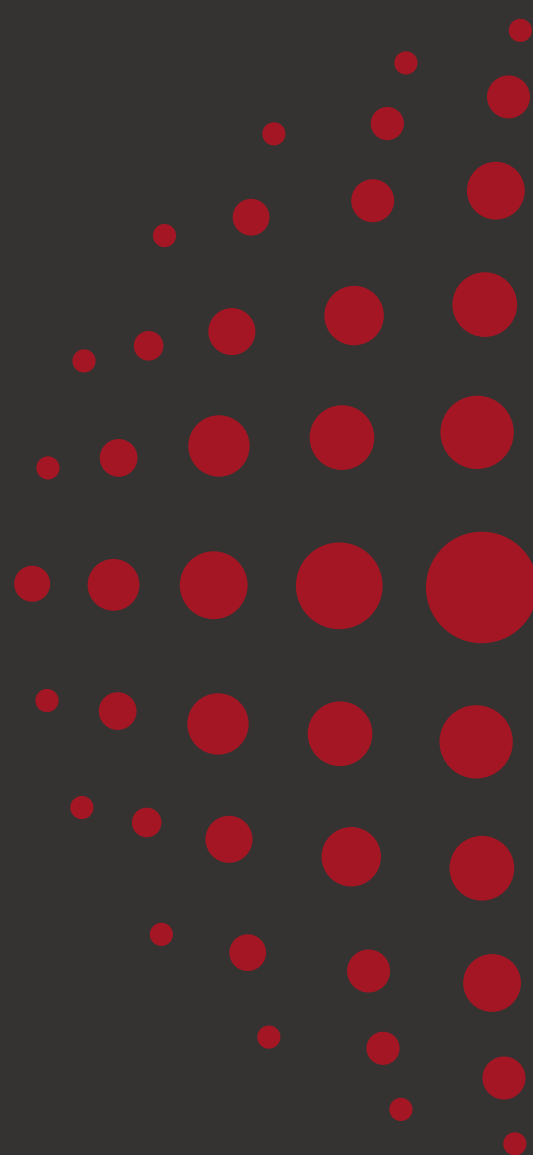
³⁰ Section 3 of the Contracts (Rights of Third Parties) Ordinance (Cap 623);

³¹ Section 4 of the Contracts (Rights of Third Parties) Ordinance (Cap 623);

³² Section 5 of the Contracts (Rights of Third Parties) Ordinance (Cap 623);

relationship stated. The parties should also remain cognisant of the engaged person's scope of work throughout the service period, and regular checks and review should be in place to ensure the scope of work and service, remain consistent to the service relationship as stated in the contract. The parties who conduct themselves in a manner that properly reflects their true intention as to the nature of their relationship during the day-to-day management can also help to avoid any potential adverse consequences on re-characterization.

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I. OVERVIEW

a. Introduction

The employment relationship is more burdensome for companies, both administratively and financially (for example: tax and social contributions), than a civil law contract (i.e. an independent contractor). Employers may therefore be tempted to disguise an employment relationship as an independent contractor relationship; a move which may result in severe financial penalties from the courts.

Parties are free to choose which type of contract they want to engage in, and its content. The parties may depart from the law in respect of their rights and obligations with mutual consent, unless specifically prohibited by the law. If the content of the contract, or the practice of the parties, includes at least one primary factor typical for employment, then the competent authority and the courts are entitled to classify the allegedly civil law contract as an employment contract with all of its legal and financial consequences.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Primary and secondary factors are utilised by Hungarian courts to help determine whether the relationship is one of employment or one of an independent contractor. The primary and secondary factors therefore provide a good starting point for determining the true nature of the relationship between the parties.

Primary Factors

If only one of the following primary factors is identified by the labour authority, or the court, in the practice of the parties, then their relationship will most probably qualify as one of employment. Severe sanctions may be applied if the employment has been disguised under a sham civil law contract.

Primary factors:

- specifics of the activity, tasks defined as a job description;
- personal working obligation;
- regular availability of the employee; and
- hierarchy between the parties.

Specifics of the activity, tasks defined as a job description

It is a mandatory component for an employment contract to contain a job description outlining the continuous and regular nature of the work. The job description will be defined broadly, allowing the employer to instruct the employee to perform different tasks falling within the scope of the job description. In comparison, an independent contractor works on a specific task or creates a certain product and, unlike an employee is not committed to a wide range of activities that need performing regularly.

Hungarian labour law makes it possible, by the rules of the temporary assignment of the employee, for employers to direct employees to work temporarily on tasks not defined in his/her job description. This is not considered to be an amendment to the employment contract. An independent contractor may not be unilaterally instructed to vary its contract and perform tasks not defined therein. An independent contractor's tasks can be changed only by mutual consent.

The specifics of the job description and the regularity of the tasks may induce the court to classify the relationship as one of employment. Regular work is fundamental to the employment relationship and so if the task to be done is a one-off task, or is required to be done irregularly, then it may qualify as a civil law contract, even if the contracting parties met each other through recruitment agencies.

If a person does the same task for the principal under a civil law contract and under a part-time employment contract at the same time (i.e. there are two different, parallel agreements between the parties), the court may hold the civil law contract to be a sham agreement between the parties.

Personal working obligation

An employee is not entitled to engage a subcontractor or another employee to fulfil his/her working obligations. The employee must work personally and is not authorised to choose a substitute if they are absent. It is the employer's right to engage more employees for the same task.

By law, an independent contractor may have the right to engage subcontractors to fulfil their obligations (although this right can be restricted in contract).

It must be emphasised that even when the contract entitles the independent contractor to engage a subcontractor, such provision will not exclude the possibility that the court may re-characterise the contract as an employment contract if, in practice, the subcontractor was not engaged or was appointed by the principal (i.e. the employer).

Further, the personal obligation to perform the task may be fundamental to an independent contractor, if the type of task requires it (e.g. an actor in a movie, an artist or other type of task which is strongly connected to personal performance).

Regularly availability of the employee

Employers have an obligation to provide work to their employees, and the employees are obliged to perform the work in return for their salary.

One of the most important obligations for an employee is to be regularly available at their working place no matter whether they are supplied with work by the employer or not. Breach of the availability obligation (i.e. not being at the working place at working time) entitles the employer to terminate the employment regardless of whether the employee is supplied with work or not.

Employees shall:

- appear at the place and time specified by the employer, in a condition fit for work;
- be at the employer's disposal in a condition fit for work during their working time for the purpose of performing work;
- perform work in person, with the level of professional expertise and workmanship that can be reasonably expected, in accordance with the relevant regulations, requirements, instructions and customs;
- perform work in such a way that demonstrates the trust vested in him/her for the job in question; and
- cooperate with their co-workers.

Employees may not accept and may not lay claim to any remuneration from third parties in connection with their activities performed during work, without the employer's prior consent.

Hierarchy between the parties

The employee works under the control of the employer and the employee belongs to the organisation of the employer. The structure of the organisation is usually detailed in the employer's organisational and operational rules, which define the employee's direct superior and (depending on the employee's position in the hierarchy) may authorise an employee to exercise some employer rights (e.g. to instruct and supervise other employees subordinated to him/her). If an individual has such employer rights, it usually indicates an employment relationship, unless such individual holds the managing director (or is a member of the board of directors) position at the company.

Therefore, the employment relationship can be identified by the hierarchy between the employer and the employee and the right to instruct and supervise. In contrast, there is no hierarchy in the contractual relationship with an independent contractor because the parties are equal and not subordinated.

The independent contractor may receive instructions, but in such case the instructions are generic. The independent contractor is entitled to decide how to perform the task.

There is also a distinction between an employee and an independent contractor regarding the right of supervision and inspection. In case of employment, the employer is entitled to supervise and inspect all stages of the employee's work in detail. The independent contractor may also be supervised and inspected, but only once the task has concluded; not while the work is in process.

The Hungarian courts have declared, on numerous occasions, that strict hierarchy is, in practice, evidence that an employment relationship exists. In contrast, if hierarchy, the right to instruct in detail and the right to supervise do not dominate the relationship, then such relationship cannot be qualified as employment.

Secondary Factors

Identification of the secondary factors outlined below in a contractual relationship will not automatically classify the relationship as one of employment. The secondary factors can however, be used to support the notion that the nature of the relationship is in fact one of employment where one of the primary factors outlined above is present. The secondary factors are as follows:

- defined daily working hours;
- place of work;
- salary or fee;
- use of the employer's equipment, resources and raw materials;
- workplace safety; and
- agreement in writing.

Defined daily working hours

The daily working time of employees is determined, in detail, by the employer. In the case of an independent contractor, they and the principal agree only on deadlines as to when the product or services is to be delivered. The independent contractor is entitled to unilaterally define his/her working hours, timeline, and daily workload. The independent contractor must meet the final deadline but workflow management is at his/her sole discretion.

However, there are some types of employment whereby the employee is partly or totally free to regulate his/her working hours, e.g. "telework" or "home office" work, and so this factor is not decisive. "Telework" means activities performed on a regular basis at a place other than the employer's facilities, using computers and other means of information technology, where the end product is delivered by way of electronic means. Other

employees who are free to regulate their working hours are employees with flexible working hours, e.g. employees in leading positions who cannot claim compensation for their overtime.

Place of work

Although the place of work is usually specified in the employment contract, and is an essential part of the agreement between the employer and the employee, it is not a definite component of employment. In some cases, the civil law contract may also define the place of work (e.g. a construction site). Further, “telework” or “home office” employees may be permitted to choose their own place of work.

Salary or fee

The parties must specify in the employment contract the employee’s basic wage. The basic wage is the employee's regular income and it should be paid in monthly arrears, except where the results of the work can only be established after a longer period. In such cases, the employer is obliged to make an advanced payment.

For the independent contractor, the fee for the provided services is usually a one time payment. However, the contractor may ask for an advanced payment and, where there is a continuing relationship, the payment of the service fee may also be a regular one.

Hungarian law regulates the minimum salary of employees. There are two types of minimum salaries, one for unskilled employees and one for skilled employees. The employer must pay employees, at least, the minimum salary. The minimum salary amount is increased by the government every year.

In contrast, the minimum salary is not provided by law for independent contractors. Instead, the fee has to be agreed by the parties.

Use of the employer’s equipment, resources and raw materials

As a general rule, the employer provides the equipment, raw materials and resources necessary for the employees to do their work properly. In certain cases, the employee may also use his/her own devices (i.e. notebook, car) so this is not a decisive factor to establish whether the contract is a civil law contract or an employment contract.

In most cases, the independent contractor is obliged to provide the necessary equipment for the task and includes the costs incurred with the performance of the task with his/her fee for the provided services. However, any variation from this rule will not be a decisive factor when establishing whether the contract is, in fact, one of employment.

Workplace safety

The responsibility for the implementation of occupational safety and health requirements lies with the employer. In the case of an independent contractor, the principal is not obliged to comply with the safety and occupational requirements.

Agreement in writing

In contrast to civil law contracts, employment contracts may only be concluded in writing. Invalidity on the grounds of failure to provide a written contract may only be alleged by the employee within 30 days from the first day on which he/she commences work. If the relationship continues, the lack of written agreement will not preclude the court from declaring the relationship as one of employment if primary factors can be identified.

b. General Differences in Tax Treatment

Social security law

The social security contribution to be paid by employees consists of the following items:

- pension contribution;
- health insurance contribution; and
- labour market contribution.

For independent contractors, the social security contribution depends on the type of civil law contract entered into. The independent contractor will usually be required to pay pension contributions, health insurance contributions and labour market contributions.

Tax law

The employer and the independent contractor are responsible for paying social security tax. Social security tax is a newly introduced concept (adopted at the end of 2011). It does not grant social rights of allowances or subsidies (social rights are covered by individual social contributions). The tax base is identical to the tax base of personal income. Irrespective of social security tax, the employee and the contractor must pay personal income tax.

c. Differences in Benefit Entitlement

Paid holiday leave

Employees are entitled to annual vacation time (paid holiday leave). Annual vacation time in Hungary is divided into basic and extra vacation time and is due to an employee in each calendar year (subject to the time spent in work by the employee in the given year). The basic vacation time is currently 20 working days in Hungary. Eligibility to extra vacation is subject to an employee's age and the number of his/her children under 16 years of age. While vacation time (inclusive of extra vacation) shall be allocated in the year in which it is due, the parties do have the ability to agree that extra vacation time can be rolled over to the next working year.

Independent contractors are not entitled to any paid holiday leave.

Paid sick leave

Employees shall be entitled to 15 working days of sick leave per calendar year. During a period of sick leave the employee is entitled to 70 percent of his/her absence fee (which is calculated based on the employee's base wage plus the last six months average of performance wage and overtime payment).

Independent contractors are not entitled to any paid sick leave or other compensation.

Special allowances

The employer may give special allowances to the employees (e.g. Christmas presents, other benefits).

Independent contractors do not receive any special allowances.

d. Differences in Protection from Termination

The employment relationship can be terminated (i) by notice, (ii) with immediate effect, and (iii) by mutual agreement.

The employer may not terminate the employment relationship during:

- pregnancy;
- maternity leave;
- unpaid child-care leave;
- voluntary military service; or
- the first six months of IVF treatment.

In addition to the above; disabled persons, mothers and single fathers of children up to the age of three years and employees five years before their pension age are also protected (although termination is allowed in special cases as regulated by labour law).

The employee is entitled to a severance payment if the employment is terminated by the employer and the employee has three years continuous service. The minimum amount of severance payment is a one-month absence fee; the maximum amount (in case of 25 years of employment) is six months' absence fee.

The employee is not entitled to a severance payment if the reason for termination is the employee's behaviour or ability to work (except for health issues).

In contrast, the independent contractor can generally be terminated without any statutory restriction. It can be terminated by mutual agreement or by either party, with or without any reason. The contract can also be terminated with immediate effect where there has been serious breach of contractual obligations. If the termination of the contract causes damage for the other party, he/she is entitled to claim for compensation.

e. Local Limitations on Use of Independent Contractors

In Hungary, there are no limitations on the use of independent contractors.

f. Other Ramifications of Classification

If the employment contract is terminated by the employer without a proper (clear, real and in line with the real cause of the termination) reason, the employee can ask for damages from the court. The amount of such damages claimed under the title of lost income is limited to 12 months of absence fee.

Upon the application of the employee, the court shall reinstate the employment if the termination breached the equal treatment obligation, if the termination took place during a prohibited period (pregnancy, child care absence etc.), if the employee was a trade union officer or an employee representative and in some other limited cases.

An independent contractor may claim damages without legal limitation on the amount thereof, but no reinstatement of the relationship is possible.

g. Leased or Seconded Employees

Leased employees

The employer is entitled to lease an employee to another employer. There needs to be a temporary work (placement) agency, a user enterprise, and an employee who is explicitly engaged for temporary work.

The agreement between the placement agency and the user enterprise shall specify the material conditions of the placement and how the employer rights are to be shared. Employment may only be terminated by the placement agency. The agreement must be made in writing.

The employment contract between the employee and the temporary work agency shall contain a clause indicating that it was engaged for the purpose of temporary work, and shall contain a description of the work and the base wage. The contract shall also be made in writing.

The basic work and employment conditions of temporary agency workers shall be, for the duration of their assignment, the same as those available to the workers employed

by the user enterprise under an ordinary employment relationship.

Seconded employees

Employers are entitled to temporarily reassign their employees to jobs and workplaces other than what is contained in the employment contract or to another employer.

The duration of such secondment may not exceed a total of 44 working days or 352 scheduled hours during a calendar year. This shall be pro-rated if the employment relationship commenced during the year, if it was entered into for a fixed term, and in cases of irregular daily working time or part-time work. The affected employee shall be informed on the expected duration of the secondment.

An employee may not be transferred to work at another location without their consent:

- from the time she learns she is pregnant until her child reaches three years of age;
- until the child reaches sixteen years of age, in case of a single parent;
- if providing long-term care personally for a close relative; or
- if having suffered a degree of health impairment of at least 50 per cent as diagnosed by the body of rehabilitation experts.

The employee shall be entitled to the wage prescribed for the job in question, or at least to the base wage fixed in the employment contract.

h. Regulations of the Different Categories of Contracts

One of the main differences between employment contracts and civil law contracts is that an employment contract must be in writing. However, it is also advisable to provide a written contract for independent contractors.

Beside the difference in formalities, the Hungarian labour law prescribes several mandatory terms and conditions in relation to the employment contract (e.g. the base wage and the job position). For independent contractors, there is usually no specific legal requirement regarding the terms and conditions of the contract.

In addition to the above, the employer must meet several requirements in relation to the employment relationship. For example, the employer must comply with occupational safety and health requirements. The employee's fitness for the job for which he is being considered shall be examined, free of charge, before taking up work and on a regular basis during the life of the employment relationship. Where there are disabled employees, appropriate steps shall be taken to ensure that reasonable allowances are made to accommodate the disability.

All the mandatory provisions are for the protection of employees.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As described earlier, the Hungarian labour courts developed several factors which are applicable for classifying the type of contract between parties. As employees are entitled to a higher level of protection than an independent contractor, labelling a civil law contract as an employment contract may have material consequences.

In Hungary, the tax authority, the labour authority and the courts are also authorised to re-classify civil law contracts as employment contracts.

The tax authority starts to review the relationship based on the following:

- notification by the other contracting party about the alleged sham contract;
- official request from the labour authority;
- results of other investigations; and/or
- data received from the contractors (income, expenses, payments).

Both the tax authority and labour authority base the review on the factors described above.

b. The Legal Consequences of Re-Characterisation

It is a general rule that the contract should be categorised based on its content, instead of its name. Parties are free to engage in any agreements but they must meet the legal requirements regarding the content of their agreements.

A sham contract shall be null and void, and if such contract is intended to disguise another contract, the rights and obligations of the parties are determined on the basis of the disguised contract.

The labour authority is authorised to fine the employer.

Where a contract is found to be a sham, the employer must pay the following:

- social security contributions (health and pension);
- labour market contributions;
- personal income tax;
- reimbursement of amount unduly paid (e.g. VAT);
- default interest; and
- penalties for engaging in a sham contract.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Any agreement that infringes upon any employment regulation, or is entered into by way of circumvention of any employment regulation or is manifestly in contradiction with good morals shall be null and void. If annulled, an agreement shall be considered void, unless the relevant employment regulation stipulates other legal consequences. The party concerned may allege the invalidity of an annulled contract without a time limit, but the statutory time of limitation for any employment claim is three years. The court may determine the invalidity of the agreement on its own motion.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Sham agreements shall be null and void, and if such agreement is intended to disguise another agreement, it shall be judged on the basis of the disguised agreement. If the authority or the court re-characterise the civil law contract as an employment contract, the independent contractor and the principal shall pay all contributions and taxes that should be paid, plus default interest and any penalty.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

In Hungarian law, the mandatory provisions of a civil law contract are not regulated. The

law does not require that the parties conclude the agreement in written form. However, to avoid any misunderstanding in case of disputes, it is highly recommended to ensure the agreement is in writing. Parties must avoid including provisions in a civil law contract that are only applicable for employment relationships, for example:

- fixed monthly payments;
- instructions on daily working hours;
- instructions on how to work;
- detailed scope of the activity;
- annual holiday days;
- hierarchy between the parties; and/or
- exact workplace.

b. Day-to-Day Management of the Relationship

As the court (in case of a dispute about the nature of the relationship) routinely examines the parties' relationship which was realised in practice, if the principal wants to avoid the re-characterisation of the civil law contract, it should avoid any practice which has any of the primary factors of employment as described above.

V. TRENDS AND SPECIFIC CASES

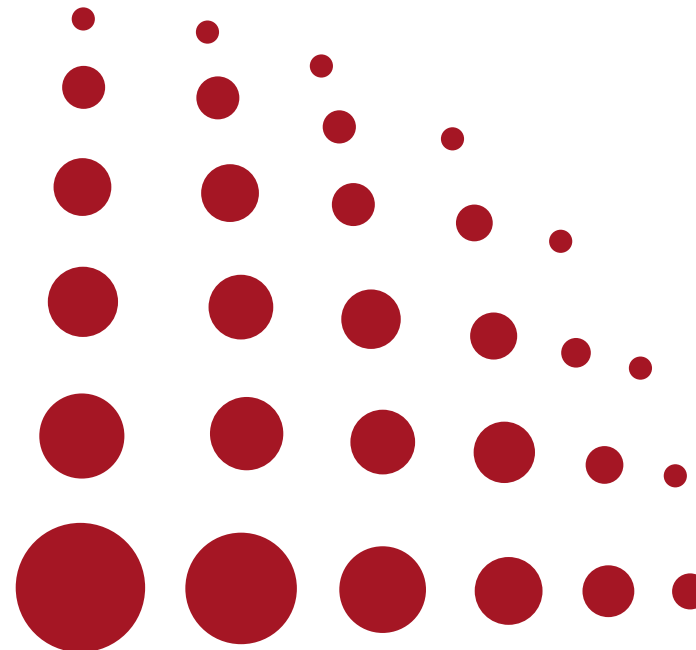
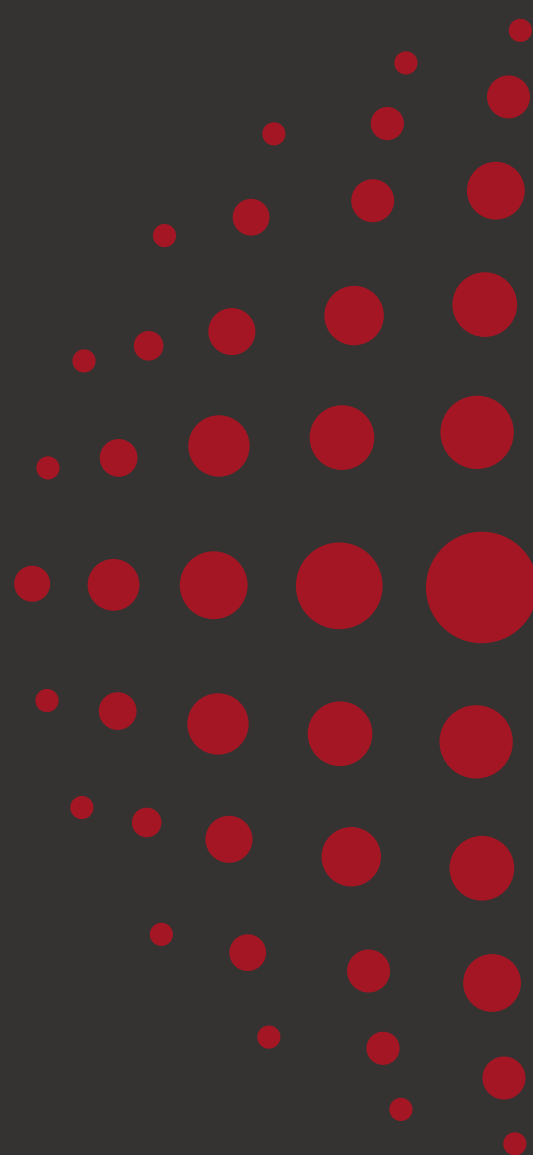
As mentioned above, Hungarian authorities and the courts are entitled to re-characterise contracts. The taxes and social contributions are higher in cases of employment relationships. The employer's obligations for employees (e.g. when terminating the relationship) are more onerous. Thus, independent contractor relationships are more popular but the authorities and the courts can easily detect the sham agreements if in dispute.

The Hungarian courts have frequently re-characterised independent contracts in the previous years. However, if the details of the relationship did not show the primary employment factors, then the courts have refused to qualify it as employment. For example, in a case where accountants worked for fixed monthly fees, for 10-20 hours per month, partly in the principal's office, and partly at home, the Supreme Court decided that the relationship was an independent contractor relationship due to the lack of hierarchy and lack of detailed instruction.

VI. CONCLUSION

In Hungary, it is sometimes hard to decide whether the employment contract or civil law contract would be better for the parties. As the financial burdens of employment are higher, it is tempting for both parties to engage using a civil law contract. However, if there is a dispute (typically in case of a termination) the independent contractor is also tempted by the possibility to raise claims under employment law due to the higher protection provided to employees. As the re-characterisation may incur severe sanctions, parties must be very careful when deciding which contract to use. The factors that have been developed by the Hungarian courts may help them to make the right choice.

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INDIA

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I. OVERVIEW

a. Introduction

The practice of engaging contractors by employers is prevalent throughout India, similar to various other jurisdictions, for improving their overall competitiveness in the globalised market economy. Increasing labour cost and the need for flexibility in managing manpower to respond to market conditions and customers' demands have caused employers to prefer contractors in a number of circumstances. However, the employment of contractors is subject to certain risks wherein such contractors may be reclassified and deemed to be direct employees of the employer in specific situations. This article provides an overview of the distinction between Independent Contractors and employees, the law governing the employment of contractors in India and the allied risks of reclassification of such contractors as direct employees.

In India, there is a distinction between a 'contract of service' and a 'contract for service'. It is on the basis of the nature of the engagement that one can be classified as an employee or independent contractor. A contract of service implies relationship of master and servant, involving an obligation to obey orders in the work to be performed, its mode and manner of performance.¹ In a case of contract of service, there may be a distinction with respect to workmen and managers. Section 2(s) of the Industrial Disputes Act, 1947 (the "ID Act") defines workman as a person employed in any industry to do any manual, unskilled, skilled, technical, operational, clerical or supervisory work, for hire or reward, terms of employment be express or implied. It specifically excludes those employed in mainly managerial or administrative and supervisory capacity.

A contract for services implies an agreement wherein one party undertakes to provide services, to or for another in the performance of which he is not subject to detailed direction and control but exercises professional or technical skill and uses his own knowledge and discretion. A reference to independent contractor may include consultants, freelancers and also contract labourers. In case of independent contractors, the relationship will be governed by the terms and conditions of an agreement, whereas, in case of a relationship with a contract labourer, it will be governed by the provisions of the Contract Labour (Regulation and Abolition) Act, 1970 (the "Act"). Under the Act, the employer is termed as a 'Principal Employer', the employees of the contractor-employer are termed as 'Contract Labour' and the agency/company that supplies such contractor employees to the employer is termed as the 'Contractor'.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The courts in India have applied the control and integration test to determine whether a person can be classified as an employee or independent contractor. The prima facie test is the **control test** to determine whether a master-servant relationship exists and it is not merely to direct the nature of work that has to be carried out but also to control the manner in which it is done. The nature and extent of such control may vary in different businesses and by its very nature is incapable of being precisely defined.²

The integration test plays a vital role in determining whether a person is fully integrated into the employer's concern or remains independent of it. Another factor, which has been considered, is whether the payment of salary is by the principal employer

¹ Indian Medical Association v. V.P. Shantha & Ors., 1995 SCC (6) 651

² Parimal Chandra Raha and Others v. Life Insurance Corporation of India and Ors., 1995 SCC Supl. (2) 611.

or the contractor³. Also, all the relevant facts and circumstances are to be considered including the terms and conditions of the agreement.

Though the control test has been considered as one of the decisive factors, the Supreme Court has decided that it is not the only test. Further, it was decided by the courts that several factors should also be considered which would have a bearing on the result such as: (a) who is appointing authority; (b) who is the pay master; (c) who can dismiss; (d) how long alternative service lasts; (e) the extent of control and supervision; (f) the nature of the job, e.g. whether, it is professional or skilled work; (g) nature of establishment and (h) the right to reject.⁴

In another case decided by the Supreme Court, the Court took into consideration an intricate factor such as who provided the equipment for completion of work. The Court held that if the employer provides the equipment, it can be considered as a contract of service. Further, the Court substantiated that if the independent contractor is using the employer's tools especially if it is of substantial value, it is normally understood that he will follow the directions of the owner in their use and this indicates that the owner is the master and therefore the employer.⁵

b. General Differences in Tax Treatment

An employer is required to withhold tax at the time of payment of salary to employees. The salary paid to an employee may include benefits and allowances that the employee is entitled to, which is beneficial to the employee from a tax perspective. However, with respect to independent contractors, the employer must withhold the applicable taxes; however, the amount paid may not be in the form of salary, but as professional fees for services performed. In both these cases, the employee and independent contractor/s will be required to file their income tax returns as prescribed under law.

c. Differences in Benefit Entitlement

An independent contractor is not statutorily entitled to any benefits. It is the terms of the agreement for service that solely govern the understanding between the employer and independent contractor. Therefore, typically in such cases, the question on benefits does not arise. In contrast, employer-employee including contractor-contract labourer relationships are governed by an agreement of service and all statutory benefits apply to these relationships. The benefits include but are not limited to provident fund, pension scheme and deposit-linked insurance scheme, employee state insurance, workman's compensation, gratuity, statutory bonus, maternity benefit, leaves and holidays (either under central or state-specific laws) etc. It is imperative to note that in case of contract labourers, it is the responsibility of the contractor to ensure that the employees are receiving these benefits. It is only in the event of any default or failure of the contractor that the principal employer is held responsible.

d. Local Limitations on Use of Independent Contractors

There is no prohibition on the use of independent contractors. However, there are certain restrictions with respect to use of contract labourers. For instance, the Act prohibits employment of contract labour in certain instances and sets out that the Central/State government may prohibit employment of contract labour in any process, operation or other work in any establishment by notification in the official gazette. The Act provides

that conditions of work and benefits to contract labourers are the key factors while determining such prohibition. The other relevant factors are whether (a) the process, operation or other work is incidental to, or necessary for the industry, trade, business, manufacture or occupation; (b) it is of perennial nature; (c) it is done ordinarily through regular workmen and (d) it is sufficient to employ considerable number of whole-time workmen. As of now, there are about 80 notifications that have been issued under Section 10 of the Act.⁶

e. Deputed or Seconded Employees

Secondment (or deputation as it is known in India) is a situation whereby an employee of a company is posted to work for another company, pursuant to an understanding between the companies. The Supreme Court⁷, on the question of deputation, decided that an employee when deputed does not become an employee of the company to which he/she is deputed. A deputationist (the company to whom the employee is seconded) has a lien on the seconded's employment and as long as the lien remains with the said company the deputationist retains control over the seconded's terms and employment.

In effect, an employee who is deputed or seconded to another company remains the employee of the depute as long as he is being paid remuneration by the depute and is required to comply with the terms and conditions governing the employment relationship.

f. Regulations of the Different Categories of Contracts

As discussed earlier, employer-employee and employer-independent contractor relationships are governed by the terms and conditions of an agreement. However, the employer would be required to comply with the provisions of the ID Act if the employee is a workman. An agreement between a principal employer and contractor is governed by the provisions of the Act and all other applicable laws, to the extent of the principal employer's obligations in the event of failure of the contractor to perform the obligations of an employee.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

In India, while there are no statutory laws that expressly govern reclassification or re-characterization of contractor labourers or independent contractors as employees, the primary tests (control and integration tests) have however been laid out by the courts. Also, Courts have also laid down several factors that may amount to deemed classification as mentioned in section II (a).

Further, please note that if a contract labourer is providing continuous service to the principal employer for more than 240 days in a calendar year, then the contract labourer may be deemed a permanent employee. That said, the Court will also take into account the kind of job profile/responsibilities with reference to the business of the organisation to arrive at the decision as the 240 days benchmark alone cannot be the sole criterion for evaluating whether the contract labourer should be considered as a permanent employee.

³ General Manager (OSD), Bengal Nagpur Cotton Mills, Rajnandgaon v. Bharat Lal and Anr., 2011 (1) SLR 140 (SC).

⁴ Workmen of Nilgiri Coop. Mkt. Society Ltd. v. State of Tamil Nadu and Ors., AIR 2004 SC 1639.

⁵ Silver Jubilee Tailoring House and Others v. Chief Inspector of Shops and Establishments and another, 1974 SCR (1) 747

⁶ <http://www.labour.gov.in/mol/NOTIFICATIONS/ISSUEDUNDERSECTION10OFTHECONTRACTLABOUR.html> (last accessed on December 7, 2016)

⁷ Morgan Stanley and Co., In Re, 2006 (284) ITR 260 (SC).

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

A contract for service, entered into with independent contractors, should ensure the following:

- the contract should be structured such that it is not construed as a contract of service.
- the employer should not exercise any overt form of control or direct the manner and process in which the services under the contract should be performed. That said, the employer may lay down the qualifications or skills to be possessed by the contract labourers.
- with respect to payments, the consideration paid to an independent contractor should not be paid as a salary since it may indicate that the relationship is one for contract for service. Further, all payments to a contractor should only be made to the contractor and not directly to the contract labourers. Any payment made directly to a contract labourer will result in the employer being considered as the principal employer.
- with regard to both independent contractors and contractor labourers, the employer/principal employer should ensure that they are treated differently from their own permanent employees. In the event that the employer is providing similar benefits, enforcing similar policies or engaging the independent contractor or contractor labourer to undertake similar tasks, such a contract may give the appearance of a contract of service.
- it is highly recommended that the benefits that are generally provided to permanent employees should not be provided to the individual contractors/consultants.
- the contract of service should specifically provide for a termination clause permitting termination without cause, such that there is no obligation to ascribe reasons to the independent contractors and contractors.
- the agreement should clearly state that the principal employer will not direct or control the contract labour and the manner in which the work should be performed, subject of course to satisfaction of certain required quality controls and customisations desired by the principal employer.

b. Day-to-Day Management of the Relationship

A contract for service should be devoid of any kind of control or supervision from the principal employer or employer, as the case may be. Therefore, such employers should avoid involvement in day-to-day management of the work undertaken by the independent contractors and contract labourers.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Under current rules, a contract labour license is granted to a contractor-employer, subject to certain conditions. One of the conditions is that the wage rates payable to the workmen by the contractor-employer must not be less than the rates prescribed under the Minimum Wages Act, 1948 or rates not less than the rates so fixed by an agreement, settlement or award, not less than the rates so fixed. The draft Contract Labour (Regulation and Abolition) Central (Amendment) Rules, 2016, propose that Rule 25 (2) (iv) be amended to include an additional condition – the rates prescribed under the Minimum Wages Act, 1948 for such employment where applicable or the rates, if any, fixed by agreement, settlement or award or 10,000 rupees, whichever is higher.

These rules are not yet in force.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors and Individuals Creates a Permanent Establishment in Country and the Ramifications

A permanent establishment in India is a fixed place of business, wholly or partly carried out by a foreign enterprise operating in India. A permanent establishment is said to have been established in India if a foreign company carries on business in India through a branch, sales office etc., or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts, or regularly delivers goods or merchandise, or habitually secures orders in India, on behalf of the non-resident principal.

Further, the Supreme Court of India has laid down certain tests to determine whether a permanent establishment is created, all of which must be satisfied in order for a foreign entity to have a tax exposure in India. These are:

- that the local entity must carry on its business from a fixed place in India (**Fixed Place Test**), however, activities of a preparatory or auxiliary character or provision of support services from such fixed place
- would not result in the creation of a “permanent establishment”; that the local entity should be an “agent” of the foreign entity, having powers to enter into contracts which would bind the foreign entity (**Agency Test**); and
- that the employees of the local entity provide services to and are under the direct supervision and control of the foreign entity through a fixed place of business in India (**Services Test**).

The Supreme Court in 2007 dealt with an issue on the nature of services performed by employees of a multinational enterprise rendering services in their overseas group companies and whether their services can constitute a Permanent Establishment (the “PE”). The Court held that when the nature of services is such that the parent company has control over the employees rendering services in the group companies with respect to payrolls and other terms of employment, such services will constitute a PE. Further, if the employees are only rendering specific services in the overseas group company following which they are repatriated to the parent company they are not employees of the overseas group company. Even if the group company exercises control over the activities of the employees, they still continue to be employees of the parent entity and thus a service PE will be established. Where the employees are monitoring the activities of the group company to ensure compliance with requirements of the parent company and there is no involvement in the day-to-day management in any specific services to be undertaken, such activities will not constitute a PE.⁸

Though, this is the general position on PE, the position may significantly differ based on the Double Taxation Avoidance Agreement (the “DTAA”) entered into between India and the foreign country. For instance, in the Indo-United States of America DTAA, there is a specific exception with reference to instances where technical or consultancy services provided are ancillary and subsidiary to the primary services for which royalties are received by a company; or making available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design.

⁸ M/s DIT (International Taxation), Mumbai v. M/s Morgan Stanley & Co. INC, Civil Appeal No. 2914 of 2007 (arising out of S.L.P. (C) No. 12907 of 2006) and Civil Appeal No. 2915 of 2007 (arising out of S.L.P. (C) No. 16163 of 2006).

VII. CONCLUSION

In order to determine whether a person is an employee or an independent contractor, the control test and the integration test together with the terms of the written agreement should be taken into consideration. Further, when having to distinguish between an employee and an independent contractor, the structure of the agreement is of utmost importance.

INDUSLAW

Avik Biswas

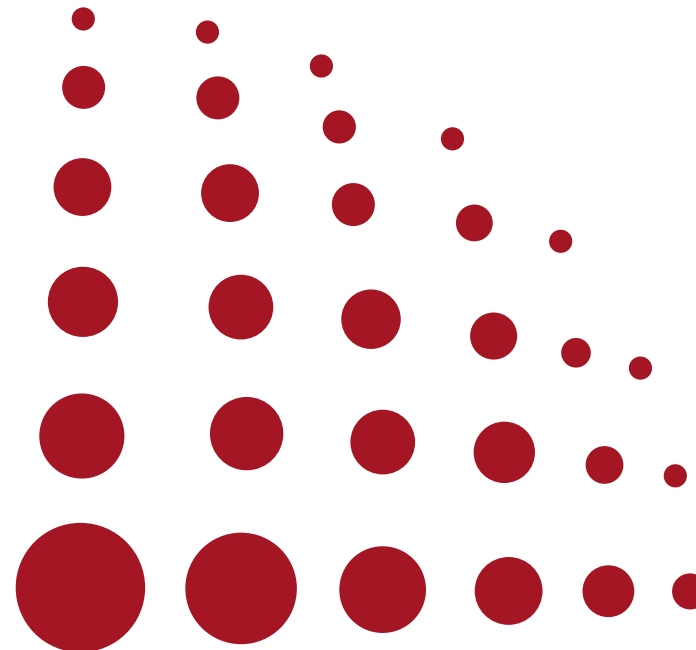
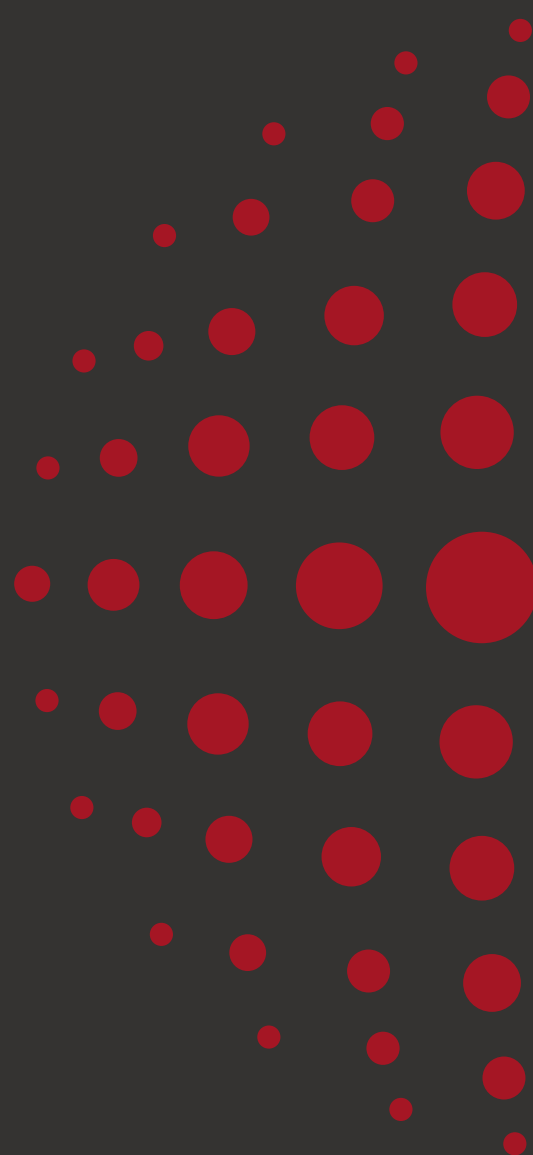
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ITALY

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I. OVERVIEW

a. Introduction

While the Italian legislator is making several law reforms to reduce unemployment rate, trying to promote the open-ended employment agreements, the utilization of bogus self-employment contracts is still widespread and the best way to regulate this is clarifying the distinction between employment and self-employment relationship.

The distinction between employment and self-employment relationship is of fundamental importance under Italian employment law, from a number of different perspectives such as employer's power, welfare and social security rights, protections in the event of termination, illness etc.

In light of the above, it is very important to define the main features of the two contractual figures because, under Italian labor law, a relationship is either considered subordinate employment or self-employment according to the way in which the relationship has effectively been implemented and managed, which always prevails over the name given to the contract by the parties (*i.e. nomen iuris*).

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The Italian Civil Code defines an employee as a person who commits himself/herself for remuneration, to cooperate in the company's business by contributing his/her manual and/or intellectual activity in the service and under the control of the employer. This means that the main features of employment are cooperation¹ and subordination.²

Therefore, the main feature of the subordinate employment is that the employee is subject to the employer's organizational, directive and disciplinary powers.

Further additional features which help identifying a subordinate employment, identified by Case law, are the absence of any business risk on the employees, the obligation to follow a fixed working time, to justify absences and agree holidays, a fixed (meaning not related to the achievement of targets) salary paid at fixed deadline.

Employees are mainly divided into: open-ended/fixed-term employees, full time/part-time employees, and apprentices (an apprenticeship contract is aimed at both training and employing young people. At the end of the contract, if none of the parties withdraw, the relationship continues as an open-ended employment relationship).

Pursuant to the Italian Civil Code, an independent contractor (or self-employed person) is a person who undertakes to perform a job or a service for a consideration, without being under the principal party's control and supervision.

In the field of the distinction between subordinate employment and self-employment, we should also take into account the employment contract belonging to the grey area between self-employment and subordinate employment such as the coordinated and continuous collaborations ("*Co.Co.Co*") and the project-based contract, which is

¹ Cooperation: pursuant to some legal scholars, it means the employees fitting into the company's organisation in a committed and systematic way.

² Subordination: is defined as the employee being subject to the instructions that are given by the employer or by other employees under whose control he/she works. As a consequence, with respect to the contractual and legal provisions, employees have to perform their duties and carry out their work in a way that is established by the employer.

a particular form of collaboration characterized by elements of the self-employment relationship and elements of the subordinate employment relationship.

In the last year, the grey area has been deeply reviewed: from the one hand, the Italian legislator eliminated the project-based contract and, on the other hand, starting from 1 January 2016 the Italian legislator changed the rules governing the “Co.Co.Co” and the VAT consultancy contracts, considering subordinate employment the contractual relationships providing personal and continuous work activities which are regulated and organized, also in relation to timing and workplace, by the employer, except for:

- collaboration relationships envisaged and governed by collective bargaining agreements aimed at meeting the productive and organisational needs of specific sectors;
- forms of collaboration provided for in the framework of intellectual professions for which enrolment in specific professional registers is required;
- forms of collaboration provided by members of boards of directors or of audit committees of businesses;
- forms of collaboration provided in the sports sector.

Always in order to make the open-ended employment contract the regular form of employment, the Legislative Decree no. 81/2015 has provided that from 1 January 2016 employers entering into a permanent employment contract with individuals who already have a self-employment contract with the same employer, are entitled to the cancellation of the tax, social security contribution and administrative violations committed in relation to the misclassification of the working relationship, if the employee signs a settlement agreement with regard to the previous employment contract and, in the following 12 months from the hiring, the employer does not dismiss the employee for reasons other than just cause or subjective justified reasons.

Given the above, today, the main categories of self-employed persons are the following: freelance professionals, the so-called “VAT number consultants”, those providing coordinated and continuous collaborations (“Co.Co.Co.”) and commercial agents.

Agency contracts, are governed by the Italian Civil Code and if applicable by the Economic Collective Agreements (“ECA”) for agents.

Agents, who must be qualified and enrolled with the Chamber of Commerce, perform their activities at their own risk, undertaking to promote, in return for a commission, the execution of contracts in a specific territory, on behalf of one or more principals.

Agents must perform their activities according to the instructions received from their principal; however those instructions shall not cancel out the autonomy of the agent, who always remains a self-employed person.

Under Italian law, agency agreements may be established either for a fixed-term or an opened-term.

In case of termination, the Italian Civil Code provides for an indemnity to be granted to the agent.³

³ As a general rule, such indemnity must be paid if the agent has procured new clients or has considerably developed business with existing clients, whereas the principal is still receiving substantial advantages deriving from dealings with these clients. The indemnity is not payable under certain circumstances (e.g. when the principal terminates the contract for just cause, consisting of a contractual breach so serious as to prevent the continuation of the agency relationship even on a provisional basis; when the agent transfers the contract to a third party with the consent of the principal). The amount of the indemnity can be equal to one year's worth of commissions maximum, calculated, as a general rule, on the average of the last five years of the relationship. The exact measure depends on the entity and number of clients and on the development of the business by the agent.

Social security contributions with ENASARCO, (the national institution providing assistance and welfare to trade representative and agents and their families) are compulsory for all commercial agents who perform their activity in Italy. The principal must enroll the agent with ENASARCO, which (i) provides social security benefits to agents in addition to the pension treatment granted by INPS, and (ii) pays to agents a part of the termination indemnity (so called FIRR) upon expiration or termination of the agency agreement for any reason whatsoever.

The applicable principles in order to distinguish an employee from an independent contractor can be found in case law.

The Courts constantly reiterate that, in principle, every activity may be indifferently fulfilled based on an employment relationship, rather than a self-employed one.

This means that the distinction between an employee and an independent contractor consists not in the kind of activity, but rather in the way in which it is performed.

The employment relationship is regulated by the provisions set forth by Sections 2104⁴ and 2106⁵ of the Italian Civil Code (while, vice versa, such provisions are not applicable to a self-employed relationship).

In particular, a worker is considered an employee if he/she is subject to the directive, organizational and disciplinary power of the employer. These powers consist in the employer giving specific orders as well as the exercise of a constant activity of vigilance and control on the execution of the employee's duties, and in the giving of sanctions in case of breaches made by the latter.

On the other hand, the contractual typology formally chosen by the parties, and other criteria like the continuity of the activity, adhering to a predetermined working time, the appointment of a fixed workspace within the employer's premises, the payment of an agreed remuneration at fixed intervals, the absence of an even minimal business structure (by the worker), are complementary to and of secondary value in qualifying the relationship.

Such criteria, however, could on the contrary, be considered decisive in case of duties which, given their intellectual nature, rather than the fact that they are merely repetitive, cannot be subject to a continuous supervision by the employer/principal.

b. General Differences in Tax Treatment

Employee's remuneration is subject to income tax (the so-called IRPEF). The employer, acting as a withholding agent, must withhold IRPEF as well as other local taxes in the pay slip and then pay them to the tax authorities.

The same applies to self-employment, although the remuneration of independent contractors also attracts VAT, payable by the principal. Social security contributions for employees are around 33% of the employee's remuneration; around 10% borne by the employee, the remaining 23% by the employer. The employer withholds the amount from the employee's pay slip and is responsible for making payment to the relevant public bodies (INPS and INAIL). The employer will incur administrative sanctions for the delay or omission in payment.

⁴ According to its subsection no. 2, the employee «must (...) observe the dispositions on the execution and the discipline in the place of work, given by the employer and his supervisors».

⁵ Such Section provides that the employee's violation of his/her duties of diligence, obedience and loyalty «may determine the application of disciplinary sanctions, on the basis of the seriousness of the infraction».

With regard to independent contractors, generally the remuneration paid corresponds to the actual company cost, since social security contributions are then directly paid by the independent contractor (in certain cases the principal may be required to pay the worker a contribution towards social security contributions of around 4%. There is a peculiarity here in that for the so-called Co.Co.Co.'s workers, although considered independent contractors, two thirds of social security contributions (around 28%) are due by the principal, who is also responsible for payment to INPS and INAIL of all such contributions.

c. Differences in Benefit Entitlement

In general, mandatory benefits provided for by the law or by the collective agreements in favor of employees (holidays, sickness and injury benefit, company car, PC or cell phone, etc.) do not apply to self-employed persons, who are compelled to perform their activity properly organizing the required time and all the necessary means, accepting all the relevant hazards.

For as regard parental leave anyway, the Jobs Act has finally provided measures to support parental care, by extending paternity leaves to all categories of workers. Plus, self-employed workers will be receiving maternity allowances even when employers did not pay contributions associated with their work.

The principal and independent contractor may however agree on specific benefits and in cases, even more favorable than those indicated above.

Furthermore, Co.Co.Co.'s. workers are entitled to be treated similarly to employees in this regard.

d. Differences in Protection from Termination

From an Italian employment law perspective, the real differentiating factor between employees and self-employed persons can be found in the context of unfair termination of the respective relationships. Employees hired under an open-ended contract are strongly protected by the law.

In fact, the dismissal of an employee hired under an open-ended contract can be grounded only on a just cause (Art. 2119 of the Italian Civil Code) which is when occurs a cause that does not allow the working relation to continue even on a provisional basis (no notice) or when occurs a justified reason (Art. 3 of Law no. 694/1966) distinguished in subjective (serious breach of contract) and objective (corporate reasons or in any case reasons not related to the employee's conduct).). This latter type of dismissal compels the employer to give the employee the notice period provided for by the applicable collective agreements, or to pay him/her the relevant payment in lieu of.

Dismissals must be served in writing

The employee may challenge the termination by filing a lawsuit within a maximum of 240 days from the date of the dismissal. In particular, pursuant to Art. 6 of Law no. 604/1966, the worker who wants challenge the dismissal as unfair has 60 days, starting from the receipt of the dismissal letter, to challenge the dismissal Out-of-Court (usually by way of a lawyer's letter) and a further 180 days to file a Court claim. Please find below a brief outline of the consequences of dismissal held as unfounded in Court:

REASON	REMEDY
COMPANIES WITH NO MORE THAN 15 EMPLOYEES	
EMPLOYEES HIRED BEFORE 7TH MARCH 2015 Dismissal null and void (e.g. retaliatory, oral)	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (min. 5 months' salaries)
Dismissal for just cause or subjective/objective justified reason held as unfounded	Reinstatement or indemnity ranging between 2,5 and 6 months' salaries
EMPLOYEES HIRED AFTER 7TH MARCH 2015 Dismissal null and void (e.g. retaliatory, oral)	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (min. 5 months' salaries)
Dismissal for just cause or subjective/objective justified reason held as unfounded	Indemnity equal to 1 month's salary for each year of length of service within the company (max 6 months' salaries)
Dismissal for just cause or subjective/objective justified reason with formal defects	Indemnity equal to 0,5 month's salary for each year of length of service within the company (max 6 months' salaries)
COMPANIES WITH MORE THAN 15 EMPLOYEES	
EMPLOYEES HIRED BEFORE 7TH MARCH 2015 Dismissal null and void (e.g. retaliatory, oral)	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (min. 5 months' salaries)
Dismissal for just cause or subjective justified reason where the allegations are not existent or punished with a minor sanction according to NCBA; dismissal for objective justified reason held as evidently not existent	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (max 12 months' salaries)
Dismissal for just cause or subjective/objective justified reason held as unfounded	Damages ranging between 12 and 24 months' salaries
Dismissal for just cause or subjective/objective justified reason with formal defects	Damages ranging between 6 and 12 months' salaries
EMPLOYEES HIRED AFTER 7TH MARCH 2015 (When a company with no more than 15 employees on 7th March 2015, exceeds such threshold through new employees hired, on open-ended basis, after 7th March 2015, the protection system described below will apply to all its open-ended employees, also those hired before 7th March 2015)	
Dismissal null and void (e.g. retaliatory, oral)	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (min. 5 months' salaries)
Dismissal for just cause or subjective justified reason where the fact alleged does not exist	Reinstatement (or 15 months' salaries) + damages equal to salaries lost as of the dismissal until the reinstatement (max 12 months' salaries)
Dismissal for just cause or subjective/objective justified reason held as unfounded	Indemnity equal to 2 months' salaries for each year of length of service within the company (min 4 max 24 months' salaries)
Dismissal for just cause or subjective/objective justified of reason with formal defects	Indemnity equal to 1 month's salary for each year length of service within the company (min 2 max 12 months' salaries)

On the other hand, except for contractual provisions to the contrary, the principal may always freely terminate an open-ended self-employment relationship.

The independent contractor is generally not granted any specific protection against the termination of his/her relationship (except in some cases the right to be given a notice period or to be paid the relevant payment in lieu thereof, or the right to be paid some particular indemnities - see the agency contracts).

Whereas in the case of a fixed-term relationship, regardless of its nature (employment or self-employment) the employer/principa⁶ cannot withdraw until the expiry date, except for (i) where there is a just cause for termination or, in project-based contracts, where the collaborator matter-of-factly shows his/her professional unfitness, (ii) cases which were specifically identified in the contract, and (iii) the general remedies against the non-performance provided for in the Italian Civil Code.

The so-called termination *ante tempus* (that is, before the expiry date) by the employer/principal entitles the employee/self-employee to claim the remuneration due until the natural expiry date.

e. Local Limitations on Use of Independent Contractors

With regard to the limitations on the use of independent contractors, Italian employment law does not establish particular restrictions, even from a quantitative point of view, in compliance with the principle, provided for by the Italian Constitution regarding freedom of economic enterprise granted to the employer.

The applicable collective agreements may however fix the maximum percentage of independent contractors (in particular for workers on project-based contracts) in relation to the total workforce.

f. Other Ramifications of Classification

There are some important ramifications of the classification, such as:

- self-employed persons are not entitled to temporary lay-offs schemes;
- self-employed persons cannot exercise union rights in the workplace, as provided for by Law no. 300/1970;
- if an employer becomes insolvent, its employees take priority over the other creditors (including self-employed persons) for unpaid remuneration and social security contributions.

g. Leased or Seconded Employees

The use by an employer of employees hired by another employer is possible, but only in the ways and within the limits provided for by Italian employment law, since in general the "leasing" of manpower is not permitted.

The rules on supply of labour introduced by the Legislative Decree no. 276/2003 have been replaced by Articles. 30-40 of the Legislative Decree no. 81/2015 with the implementation of Law no. 183/2014.

Through staff leasing, the user can request employment agencies authorized by the Ministry of Labor⁷ and registered in a special register, to supply manpower.

⁶ The same rule applies also to the employee/self-employed person.

⁷ In the course of the authorization process, the Ministry of Labor determines whether applicants meet the legal requirements. These requirements include minimum financial capital, adequate professional skills, and the "honorability" of directors (i.e., they should not have been convicted of criminal offenses relating to the labor law).

After the amendments of the Legislative Decree no. 81/2015, labour supply, as a commercial contract, may be:

- **fixed-term** and without technical, production, organizational and replacement reasons even if connected to the ordinary business of the user (as before);
- **open-ended**.

Unless otherwise envisaged in collective agreements, the number of workers leased under labour supply agreements on an open-ended basis may not exceed 20% of the number of permanent workers employed by the user company on 1 January of the year in which the agreement is stipulated.

The supply of workers on a fixed-term basis, meanwhile, is subject to the quantitative limits set forth in collective agreements applied by the user company.

For the duration of the placement, supplied employees perform their duties in the interests of and under the instructions and control of the user (disciplinary powers however remain with the employment agency) and are entitled to the same working conditions as those equivalent employees of the user, and are also entitled to exercise union rights.

In the case of workers engaged under open-ended contracts with the agencies, the same are entitled to a monthly indemnity for their availability, in the periods where they do not have any job.

The user is jointly liable together with the agency for the remuneration and social security contributions due to the agency employees, and is also responsible for the damages caused to third parties by such employees in the execution of their duties.

The labour supply, as described above, presents the advantage for the user that it can avail, for the period of time deemed necessary, of a person who - on one hand - is for all intents and purposes an employee (and therefore who is subject to the directive and disciplinary power, as well as to other duties like that of fidelity), but - on the other hand - is not on its pay roll.

However, the labour supply means that the user has to bear the costs of work as well as the fees related to the agency's service.

The employer may also use seconded employees.

According to Italian law (Section 30 Legislative Decree no. 276/2003), the secondment of an employee for the execution of specific duties presupposes that his/her employer has a real and actual interest in it.

Secondment is temporary; however no set maximum duration is provided for by law.

The worker's employer remains legally responsible for all the economic and regulatory treatments due to him/her during the secondment (usually, the costs are then tipped over to the other employer).

The applicable collective agreements may contain provisions regulating specific payments (e.g., the reimbursement of the relocation cost related to the secondment) to which the seconded employee is entitled, or these are agreed directly with the seconded employee. The consent of the employee to his/her secondment is not required, unless the secondment involves a change of duties.

The secondment must be necessarily justified by technical, production, organizational or replacement reasons, when it entails the transfer of the employee to a production unit located more than 50 km from the one to which he/she was assigned before the secondment.

In case of violation of the main principles applicable to secondment (interest of the worker's employer and temporary nature), the employee may claim the constitution of an open-ended employment contract with the end user of his/her services.

Finally, the employer may enter into a service agreement, through which the contracting firm's employees perform their duties in favor of the employer.

According to Section 29 of Legislative decree no. 276/2003, service contracts are characterized by the fact that the contractor organizes all the necessary means for the execution of the service or the work, assuming the business risk and exercising the organizational and directive power over its employees.

Also, in this case, the employer is allowed to (indirectly) use employees without the need to hire them, simply paying the costs for the services received, as agreed with the contractor.

However, there are possible disadvantages. Firstly, unless otherwise provided by the applicable national collective agreements, the principal is jointly and severally liable with the contractor and each eventual sub-contractor, for a period of two years from termination of the contract, to pay the employees of the contractor and/or any sub-contractors, their salaries as well as social-security contributions and insurance premiums owed in relation to the period of performance of the contract⁸. Similar joint and several liability between principal and contractor is envisaged by law (Section 26 of Legislative Decree No. 81/2008) for any workplace accidents not covered by INAIL sustained by the contractor's employees that occurred due to the violation of workplace safety statutes.

Secondly, in the absence of the elements indicating a true service contract, the contractor's employee (again) may claim the constitution of an open-ended employment contract with the principal.

New rules concerning the secondment of employees in the European Union are set forth in Legislative Decree no. 136/2016 which has implemented the EU Directive 2014/67/EU.

h. Regulations of the Different Categories of Contracts

In Italy, the different types of employment and self-employed relationships are substantially regulated by the civil code or by specific laws.

In particular, the open-ended employment relationship is governed by the civil code; while some particular aspects (working time, health and safety at work, dismissals, etc.) are governed by separate and recently enacted laws.

The characteristic elements of fixed-term, part-time and apprenticeship relationships are regulated by ad hoc laws while other rules not expressed there can be derived - if not conflicting - from the rules applicable to open-ended contracts.

Each of the self-employed relationships, instead, has its own regulation, each one is very different from the other: therefore, common roots can rarely be found.

⁸ The foregoing is obviously without prejudice to the right of the principal, after paying the sums due, to initiate recovery action against the jointly and severally liable party or parties. If sued, the principal may also invoke the benefit of prior discussion of the assets of the contractor and any sub-contractors

General civil law principles regarding obligations and contracts (the principles of correctness and good faith, resolution or suspension of the contract for intervened impossibility of the performance, etc.) may be used for both employee and self-employed relationships, in the absence of special regulations, provided that they are compatible with such relationships.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

The re-characterization of a self-employed relationship as an employment relationship is usually the result of mismanagement of the relationship. In the absence of specific regulatory provisions, the applicable principles can be found in case law.

b. The Legal Consequences of a Re-Characterisation

The main rule provides that once defects are ascertained, the relationship is converted ab origine (from the beginning) into an open-ended employment relationship. This means that the employee is entitled to the following:

- to go back to work, performing the same or similar duties;
- to any differences in remuneration between remuneration actually received and the amount due for the type of activity performed, on the basis of the provisions of the applicable collective agreements;
- to the differences between social security contributions already paid and the higher ones actually due;
- to the usual legal protections against unfair dismissal.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The re-characterization of the relationship requires the filing of "ordinary" proceedings before the employment tribunal, where the worker is required to prove he/she was subject to the directives and disciplinary power of the employer and must show other indicators of an employment relationship.

If for example, a coordinated and continuous collaboration contract is characterized by exclusively personal and continuous work activities whose methods of implementation, also in relation to timing and workplace, are organised by the employer (hetero-organization), then it is automatically converted into an open-ended employment contract pursuant to Art. 2 of Legislative Decree no. 81/2015.

When the re-characterization is connected to acquiring legal protections against unfair dismissal, such a claim has to be filed accordingly to the specific rules of the new proceedings, introduced by Law no. 92/2012, for challenges against dismissals (a proceeding specifically introduced in order to allow a quicker execution and conclusion of such lawsuits) and no longer applicable to employees hired from 7 March 2015.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The employer will face administrative sanctions for delayed payment of social security contributions in the correct measure.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Practically all self-employed contracts require a written form for two reasons: *ad substantiam* - that is, in order to have a valid contract - rather than *ad probationem* - that is, in order to allow the principal to demonstrate its existence.

Therefore, it is important to draft a contract in which the autonomous nature of the relationship is clearly expressed.

b. Day-to-Day Management of the Relationship

As we have seen, the distinguishing feature of self-employment relationship is the way of implementing the performance that must be rendered independently by the worker, without any relationship of subordination with regard to the enterprise (no subjection of the independent contractor to the executive, organizational and disciplinary power of the employer).

It follows from this that the independent contractor is, in general, entirely free to decide whether and when to work or not; this means that he/she does not have to ask for leave or holidays, nor does the principal have the power to grant them.

So, with regard to managing the relationship, the self-employed person must be permitted to fulfil his/her services without any strict controls or interference by the principal. The latter must limit its intervention to a general coordination (e.g. a few meetings per year, just to be kept informed of the performance of the services or the evaluation of the results achieved by the worker). No precise and detailed directives must be given to him/her.

In this respect, it is advisable to be very careful with written communications (above all, emails), since their meaning can be misunderstood, and later on used against the principal (as proof of the subordinate nature of the relationship).

Finally, the termination of an open-ended relationship has to be communicated in writing, avoiding comments on the performance of the worker and using a very neutral tone (so that such communication cannot be interpreted as part of a disciplinary process).

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

According to case law:

i. It is possible to be both an employee (manager) and an independent contractor (member of the board of directors) of the same company, when such person, as a manager, is subject to the control of the president and the board of directors; while, as a member of the board, does not have full powers (Supreme Court, 18 September 1995, no. 9864);

ii. With specific reference to betting shops' personnel, an employment relationship could be established even if the worker can decide whether to accept or not to work, and whether to actually come to work or not, without the need to justify such actions (Supreme Court, 5 May 2005, no. 9343);

iii. The activity performed by the so-called "pony express" can be considered that of an independent contractor if the worker uses his/her own means of transportation, bearing the relevant costs and risks, and if he/she decides all the aspects (itinerary, period of the day, etc.) connected to the deliveries (Supreme Court, 20 January 2011, no. 1238);

iv. Since the journalist's duties are characterized by a certain autonomy, an employment relationship occurs when the journalist is considered part of the company organization: that is, the journalist regularly writes articles on specific topics or columns, and he/she is available even between one assignment and the next. On the other hand, other factors like the place of work and the absence of a fixed working time are unimportant (Supreme Court, 9 September 2008, no. 22882);

v. Call-center personnel may be considered as employees if they make phone calls following directives on the number and the outcome of the same (Supreme Court, 14 April 2008, no. 9812);

vi. The communication sent by the employer to employees, clients, collaborators and suppliers, in which a consultant is qualified as responsible for a sector, and head of the sales department, cannot be considered decisive for the qualification of the relationship (Supreme Court, 27 July 2009, no. 17455);

vii. The presumption of subordination exists in the relationship between a pharmaceutical company and a pharmaceutical representative where the latter is subject to close supervision and control by his superior that deprives him of any kind of autonomy (Supreme Court, 23 October 2001, no. 13027);

viii. The job of training performed by a tennis coach in an academic sports center, where he organizes his own job, also with regard to attendance and schedules, cannot be re-characterized as an employment relationship (Supreme Court, 1 December 2008, no. 28525).

b. Recent Amendments to the Law

The recent amendments to the rules governing self-employment and CO.CO.CO. contracts, have tried to better distinguish the employment and self-employment relationships, limiting the future intervention of case law.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

Foreign employers that are interested in employing local workers may:

- establish a local company under Italian law and be represented in Italy by its legal representative; the legal representative of the company could maintain his/her establishment abroad and is liable in Italy; or
- create a branch office; in this case, the foreign employer shall need to have representation for social security purposes (by a labor consultant or a chartered accountant) in Italy.

Similar principles apply with regard to independent contractors.

VII. CONCLUSION

In Italy, at present, the main type of employment relationship is still the employee/ employer relationship and the purpose of the Italy's Jobs Act is, in fact, to render the open-term employment contract the normal form of employment, replacing the "non-genuineness" contractual forms widespread before this reform (i.e. VAT number consultants contracts and the project work contracts).

Self-employed relationships are widespread and commonly used, but sometimes they are viewed by the Courts with suspicion, as if behind them lurks a subordinate employment relationship in disguise.

Case law on this issue, however, is fairly consistent and uniform, and the principles applied in order to establish the real nature of a relationship are clear.

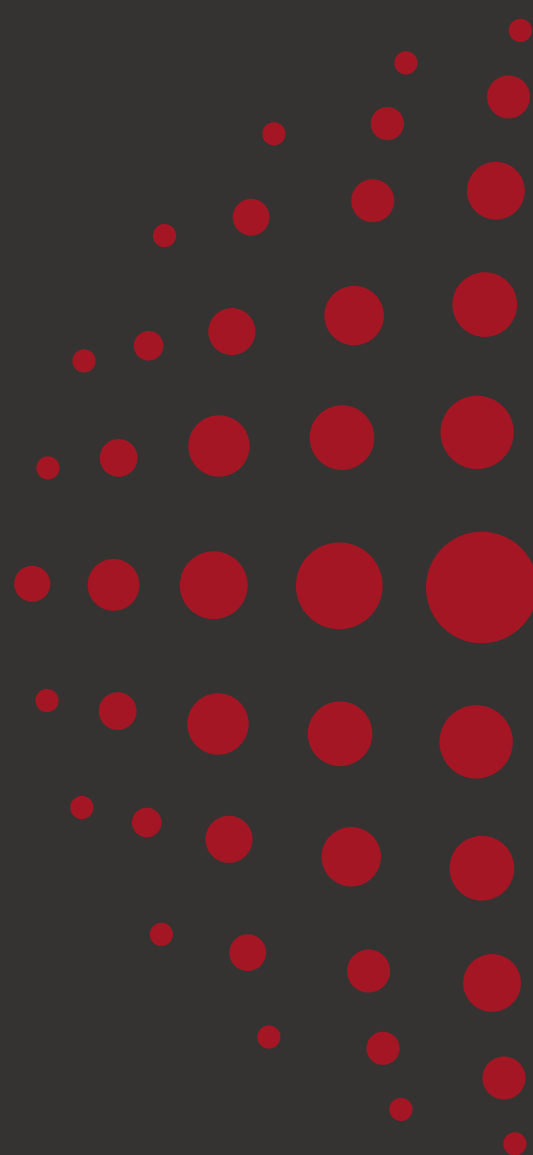
Therefore, the principal must pay particular attention to the actual management of the self-employed relationships it has entered into.

In fact, the "genuineness" of the relationship prevents the independent contractor from obtaining, after the termination of the service, a court order to come back to work in the company, this time as an employee.

LABLAW STUDIO LEGALE

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JAPAN

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I. OVERVIEW

a. Introduction

Distinction of employees and independent contractors is one of the most important issues in the workplace in Japan, due to the prevalence of what administrative authorities viewed as misuse of the usage of independent contractors by employers. A recent amendment to the Worker Dispatch Act has been implemented from October 1, 2016, which now deems that if a scheme utilizing independent contractor is considered “contractor-in-disguise” (employment done in the form of usage of an independent contractor), the recipient (client) is deemed to have offered employment to the independent contractor (if the independent contractor is a company, to its employees working for the client), so if the worker wishes to be employed, an employment contract will become established.

The one structure that is an exception is the use of dispatched workers employed by a licensed worker dispatch company. While there are a number of rules to comply with to start and continue use of labour service provided by dispatched workers, utilization of dispatched worker is one exception legally allowed to directly receive labour of non-employees.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

An independent contractor under Japanese law is a person/ entity that works as an independent service provider, and not subject to instruction or supervision by the particular business entity which is the client. In determining whether the individual working for a client is an independent contractor, the administrative authorities and courts typically consider whether the independent contractor:

- i. possesses the discretion to accept or refuse a job offer (i.e. cannot be “ordered” to work, and can choose to accept an assignment or not) – even clearer if the individual can and does take work from other client(s);
- ii. has the discretion to decide how to perform their own service and management of their work, who to allocate for the work (when the independent contractor is not an individual), and not evaluated, supervised or directly managed by the client (the client may evaluate the contractor as it would any outside contractor, but cannot discipline, demote, or otherwise evaluate in a way that is unique to employees). When detailed instructions are necessary to outsource service, this can still be done if the requirements are set out in writing, and made as part of a pre-arranged agreements, rather than instructions by the client, but direct contact for detailed/ daily instruction is one of the strongest indicator of “contractor-in-disguise”;
- iii. possesses the discretion to decide own working hours, work days as well as management of attendance;
- iv. assumes responsibility for damage regarding their own performance and otherwise all responsibilities as a business entity regarding the performance of the service;
- v. procures their own funds and makes payments necessary for the tasks assigned;
- vi. tax treatment is in line with independent contractor, such as paying consumption tax (for domestic matters and the client is a taxable entity in Japan – this may not be added for service to a foreign entity), and the individual reports the remuneration as business

income (not salary from client) for tax purposes;

vii. owns the instruments or materials to perform the work, or pays compensation for any instruments leased by the client, and does not simply provide physical labour subject to the client's supervision and order;

viii. whether or not contributions to employment insurance, workers accident compensation insurance, employment pension and employee health insurance are not deducted from the remuneration to the individual;

ix. if the individual is substitutable with others in performing the work (i.e. if the individual has the discretion to use a substitute or an assistant), it will enhance the independence status;

x. any clear difference with how employees are treated would also help clarify the status of an independent contractor.

Not fulfilling one or more of the above criteria will not necessarily mean that the relationship will automatically be viewed as an employment relationship, as long as there is a reasonable business necessity for the exception (such as having to provide services at the client's premise if the nature of the service requires it, but in such instance, the client needs to be careful not to directly give "instructions" and should be avoided as much as possible). In order to clarify that the contract fulfils the requirements for an independent contractor, there should be a written agreement to confirm the arrangement with the independent contractor.

b. General Differences in Tax Treatment

Independent contractors normally need to be paid consumption tax (for domestic matters and the client is a taxable entity in Japan – this may not be added for service to a foreign entity), to be borne by the client. Whether withholding for income tax is made for remuneration to an independent contractor depends on whether the independent contractor is incorporated or not. Remuneration to an independent contractor would be categorized differently from "salary income". Employees' remuneration, taxed as salary income, is subject to withholding of income and resident's tax.

c. Differences in Benefit Entitlement

There is no statutory obligation to provide any benefit to an independent contractor – the independent contractor is responsible for their own (or if they employee employees, their employees') benefits.

Provided, however for dispatched workers to receive access to benefits/ training opportunities that direct employees are provided as much as possible.

d. Differences in Protection from Termination

Contracts with an independent contractor is subject to the Civil Code and Commercial Code, so termination would need to meet requirements thereunder, or fall under a contractual cause for termination. There is no minimum or maximum period. While frequent renewals and/or a very extended period may lead to a client requiring a "justifiable cause" for termination, parties can exclude such a risk by having a clear agreement on what the criteria for extensions are and that the independent contractor is not given expectation of automatic renewals.

In contrast, employees, who are protected by the Labor Standards Act and Labor Contract Act, among other employee-related law, cannot be terminated without "reasonable cause" for open end employees (the term "reasonable" may be misleading, as it is not the same as "reasonableness" from what may be deduced from common sense, it requires a demonstration of a high-level difficulty to maintain employment by the employer), and "inevitable cause" for terminating a fixed term employee during their fixed term, and such strict rules cannot be changed even if the employee agrees to less stringent causes for termination in an employment contract if Japanese law applies as the most relevant law in relation to employment. Further, an amendment to the Labor Contract Act implemented in 2013 now stipulates that an employee has a right to change a fixed term employment contract to open end if a fixed term contract starting on or after April 1, 2013, reaches a period over 5 years due to renewals (please note that a fixed term employment contract as a general principle cannot be longer than 3 years – otherwise the court will assume that it turned into open end after exceeding the statutory upper limit).

e. Local Limitations on Use of Independent Contractors

Independent contractors must maintain their independence – otherwise, usage of a third party workforce is regulated, and unless the structure falls under such regulated exception, illegal.

Independence is determined by the factors listed under II.a. above. The few exceptions allowed (in other words, using labor of third parties as if the workers are employees of the Client) is to use worker dispatch from a registered worker dispatch agent, and such relationships are permitted under heavy regulation, or secondment, which is also subject to certain restrictions.

Use of third parties as part of the Client's workforce, without distinction of the independence contractor status nor fulfilling the criteria for worker dispatch or secondment, is viewed either as (i) violation of the Employment Security Act (*Shokugyo Antei Ho*) called "worker provision" under which both sender and recipient are subject to criminal fine of JPY1million or less, or (ii) violation of the Worker Dispatch Act (*Rodousha Hakenjigyo no Tekisei na Unei no Kakuho oyobi Hakenroudousha no Hogo ni kansuru Houritsu*) under which the sender may be subject to criminal penalty, and the recipient (client) would be subject to administrative guidance. Which law will apply will depend on whether the sender and recipient each have an employment relationship with the worker. If the sender employs the worker, but the recipient does not, the Worker Dispatch Act will apply; if the sender does not employ the worker, or if the sender employs the worker but the client also employs the worker, the Employment Security Act will apply.

In case of violation of the Worker Dispatch Act, the following situations will lead to "deemed offer of direct employment" by the recipient, unless the recipient can prove that they were unaware of such violation and was not negligent in not noticing the violation:

i. Having the worker engage in prohibited areas of business (e.g. port work, construction, security, medical work, certain licensed work such as lawyer, judicial scrivener, certified public accountant);

ii. Accepting dispatched worker from an agent that is not a licensed agency;

iii. Accepted a dispatched worker beyond the period allowed under law.

Periods allowed under law:

- dispatch less than 30 days is prohibited except for certain types of work (e.g. translator, secretary)
- unless the worker is employed as an open end employee at the temp staff agency, is age 60 or older, or works under certain special circumstances (such as replacement during child care/ family care leave), there is a 3 year limitation on worker dispatch that applies in two different ways.

One is that the aggregate period of accepting a dispatched worker in the same workplace will need to be within 3 years – even if the individual changes, or the position a dispatched worker is accepted for is different, as long as there is a dispatched worker in that workplace, such period will be aggregated. The 3 year period can be renewed if the employer obtains the opinion of the employee representative of the workplace on what they think of continuing accepting dispatched workers (if an employer fails to do this, and continues the use of a dispatched worker, the employer will be deemed to have offered direct employment basically with the same terms and conditions of employment which applied between the worker and the temp staff agency).

The second restriction applies if the same worker works in the same position/ team for over 3 years, again, the employer is deemed to have offered direct employment. This means unless the worker is an open end employee at the temp staff agency (or falls under other exceptions explained above), any business accepting dispatched workers must rotate them at least every 3 years to avoid starting direct employment.

The 3 year period in both cases (where the workplace continuously receives a dispatched worker for 3 years, or if the same individual works continuously as a dispatched worker for 3 years) can be interrupted by a gap longer than 3 months – however this needs to be a genuine gap and if it is obviously placed to circumvent the 3 year gap, the parties involved in worker dispatch may be viewed to be in violation of the Worker Dispatch Act, and the recipient may be obligated to offer direct employment of the worker.

f. Leased or Seconded Employees

As explained above, the use of temp staff (worker dispatch) is allowed under certain restrictions although they are not referred to as “leased” employees in Japan.

Secondment, which is defined as a relationship where the seconding entity sends its employee to a different entity, and the recipient entity either employs, or enters into a similar relationship (not necessarily full employment, but a relationship includes aspects of employment) is commonly performed in Japan, especially among group companies, but according to administrative guidance issued by the Ministry of Health, Labor and Welfare, secondment must fall under one of the following categories to avoid falling under illegal worker provision. The administrative authorities’ view is more narrow than what is done in practice, so there is a significant discrepancy between what is done as common practice and what the administrative officials view as acceptable):

- the secondment is done to avoid termination of employment, by procuring a position as an employee at a group company;
- performance of guidance in management skills or technical skills;
- part of training work related abilities;
- exchange of personnel within corporate groups.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Worker Dispatch Act, which has through an amendment implemented on October 1, 2015, introduced a deemed employment offer when the situations described above (*Local Limitations on Use of Independent Contractors*) exist.

b. The Legal Consequences of a Re-Characterisation

Deemed offer of employment under the Worker Dispatch Act:

The client is viewed to have offered direct employment with the Independent Contractor (if the Independent Contractor is an individual working directly for the Client) or the employee(s) of/ person(s) sent by the Independent Contractor (if the Independent Contractor uses the labour of individuals to provide service for the Client).

All the terms and conditions of employment that is deemed to have been offered by the client would be equivalent to the terms and conditions which previously applied if the person was employed by the Independent Contractor (e.g. if the individual was a dispatched worker from an agent, the terms and conditions of employment they had with the agency would automatically apply, including salary).

The worker can establish an employment relationship by communicating their acceptance of the deemed offer to the client. The deemed offer is valid for one year, so the worker has one year to decide and communicate their “acceptance” from the time of the last day of the illegal situation leading to deemed offer of employment.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

Workers who seek confirmation of employee status may seek this through judicial means (lawsuit, labor tribunal, arbitration). Such disputes will likely be on the rise as the year 2018 nears, as explained below (Trends and Specific Cases).

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

The most basic step to start a valid outsource relationship without incurring the risk of “contractor-in-disguise” is to have a clear agreement stipulating the purpose/ content of the service to be provided, and to detail any requirements/ instructions in either the contract or documented request to avoid daily contact regarding work requirements between the client and Independent Contractor.

The contract should also include provisions on how each party divides responsibilities and liability surrounding the work, such as the Independent Contractor bearing the fees for, and procuring the necessary equipment for carrying out the work, and if the Independent Contractor needs to rent equipment/ facility of the client, to have provisions that would make financial and business sense regarding such lease/ use of equipment.

b. Day-to-Day Management of the Relationship

All work related communication should be done in writing/ electronically through the person(s) acting as the point of contact, to avoid a situation where direct/ daily communication, which is difficult to distinguish from supervisory/ instructive relationship

seen in employment relationships.

One of the recommended requirements when the Independent Contractor works at the same site as the client is to have someone in charge to be the contact person, divide the workspace and take measures to clarify the division and independence of the Independent Contractor. A Q&A issued by the administrative authority give examples such as while the client directly providing technical training/ guidance to the Independent Contractor is prohibited, certain circumstances would be allowed without leading to a determination of “contractor-in-disguise” if the Independent Contractor needs to borrow equipment from the client and learn how to use such an equipment, to provide an introductory explanation to the workers of the Independent Contractor (under the supervision of the Independent Contractor).

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

There are two significant issues expected to arise in 2018. One is the expiry of the 3 year period which is the cap for worker dispatch, implemented on October 1, 2015, meaning that workplaces which accept dispatched workers who are not employed permanently by their dispatching agency can no longer continue working at the same client, unless they are employed on an open end basis by the dispatching agency.

The second is the impact of the revision to the Labor Contract Act implemented on April 1, 2013, which changed the rules concerning fixed term employment so that when fixed term employment which started on or after April 1, 2013, is renewed, and the aggregate period exceeds 5 years, the fixed term employee can seek open end agreement with their employer (there are a few exceptions to this rule, such as reemployment of persons over age 60). This means that the earliest timing in which the 5 year period starting from April 1, 2013 will be exceeded will be April 1, 2018.

Since many dispatched workers are employed as fixed term employees, there is a possibility that worker dispatch companies may refuse renewal of fixed term contracts before reaching a 5 year aggregate period, particularly since the worker dispatch company will need to find a new client to send the dispatched worker to after they continue to work for the same client in the same position. This will likely lead to many disputes where the validity of non-renewal of fixed term employment right before reaching the 5 year period is valid as year 2018 nears.

b. Recent Amendments to the Law

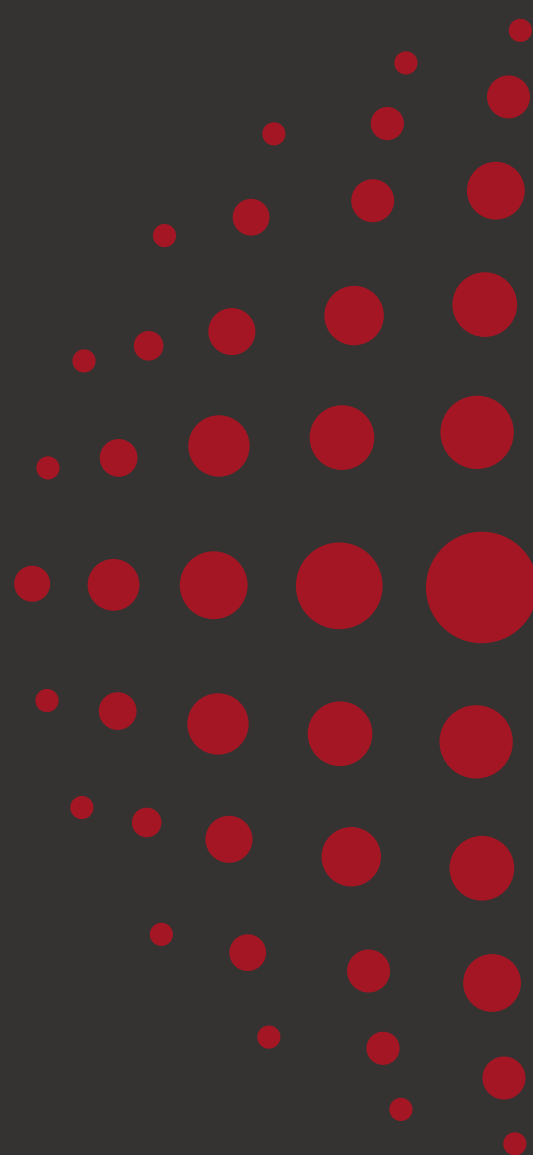
As explained above, this area of law has seen significant amendments in recent years, to promote permanent and direct employment, and restrict temporary use of labor service, as seen from the amendment to the Worker Dispatch Act which restricts worker dispatch to a maximum period of 3 years for the same individual to be dispatched for the same position, unless that worker is employed by the worker dispatch company. This provides employment security for the dispatched worker, since it had been common for worker dispatch companies to employ dispatched workers for fixed periods, and only for periods when there is a client to send the worker (so if the worker dispatch company did not have a client to send the worker, they do not have to keep employing, and paying the salary for, the worker), and this amendment promotes worker dispatch companies to employ dispatched workers on an open end basis, meaning the worker will still be employed during gap periods when there is no client to be sent to.

VI. CONCLUSION

Recent employment related amendments to the law show a tendency for legal and administrative intervention to promote more stable, permanent employment relationship by restricting the freedom of contract, freedom for employers to choose their employees, which used to exist more widely under Japanese law. Since employees in Japan are protected by extremely strict rules regarding restriction of dismissal, it has become even more important for employers to understand and comply with laws and ordinances to avoid inadvertently becoming bound by employment relationships that the employer did not choose to establish.

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MEXICO

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I. OVERVIEW

a. Introduction

As a country using a civil-law system, Mexico's labour relations were regulated under the concept of the Civil Code up to the end of the 19th century. According to the Code, labour relations were viewed as the leasing of workers, so that the worker was an independent contractor leasing his time, skills and energy to another party (natural or legal person). Consequently, at that time there was no distinction between the concept of an employee, worker or an independent contractor.

At the end of the 19th century and the beginning of the 20th century, scholars and legislators considered that the services rendered by a worker were subject to the authority of the recipient of said services; therefore, the concept of 'subordination' became a factor which differentiated services rendered on an independent basis from other labour relationships not previously contemplated under the principles of the Civil Code, and as a result, the concepts of 'worker' or 'employee' and 'employer' appeared in the legal framework.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Mexican Federal Labour Law ("FLL") defines an employment relationship as the rendering of a subordinated personal service by one person to another, in exchange for the payment of a wage and the execution of an individual employment agreement. The main characteristic of any employment relationship is subordination, which the Fourth (currently Second) Chamber of Mexico's Supreme Court of Justice has defined as the employer's legal right to control and direct the employee and the employee's corresponding duty to obey the employer. Once an employment relationship exists, all the rights and obligations under FLL automatically apply, regardless of how the agreement is characterized by the parties.

"LABOUR RELATIONSHIP. SUBORDINATION IS THE DISTINCTIVE ELEMENT OF THE RELATIONSHIP."

Article 20 of the Federal Labour Law provides that a labour relationship must be understood as the rendering of a personal, subordinated service in exchange for a salary. Therefore, a labour relationship has as distinctive element of legal subordination between employer and employee, by virtue of which the first has at any time in the opportunity to direct the work of the latter, who has the correlative obligation of obeying the employer."

Binding decision issued by the Second Collegiate Circuit Court on Labour Matters in the Fourth Circuit. Thesis IV.2°. J/1 published in the Judicial Weekly, Volume I, May, 1995, p. 289, Ninth Epoch, Record 205 158."

The employer is responsible for the execution of the agreement, which must set out the conditions under which the work is to be performed. The fact that there is no signed employment agreement does not deprive the employee of his or her rights under the law.

In other words, if an individual renders services to another person or business entity in Mexico, and the services are performed while the individual is subordinate to that other person or business entity, then the performance of those services will be considered to be a labour relationship. For purposes of the FLL, a labour relationship can derive from

the existence of a labour agreement or subordinate work (even if no labour agreement actually exists or is drafted as a professional services agreement).

The following criterion of the Supreme Court is relevant:

"If the defendant presents an objection in the sense that the relationship with the plaintiff was for provision of professional services, and offers during the labour action an agreement where this is specified, stating that the relationship is governed by the provisions of the Federal District Civil Code, this instrument in itself does not prove that the relationship was of that nature, because you need to study that document together with other evidence to solve this case - i) if during the labour action, elements of subordination are accredited, for example, the service provider is given orders about where and how his work must be performed, and is given tools which are the property of the company to perform the work; ii) if an ID identifies him as the company's employee, and he is assigned economic compensation, which even if these are called fees as recorded in the agreement, in reality it is truly the compensation paid for his work. If so, then we must conclude that the real relationship existing between the parties was an employment relationship and not a civil one."

Considering the above, from a practical standpoint, we may say that in an employment relationship the employee must be a natural person, that is, an individual who, by virtue of subordination, must render his services on an exclusive and permanent basis to the employer and be subject to the employer's command regarding the performance of his activities, including work schedule, place to perform the services, the persons to whom the services will be provided, the time period over which the services are to be provided and the continuity or regularity of the services to be provided. The employee receives a salary in exchange for the work performed.

Thus, we can summarize the differences between a labour relationship and an agreement with an independent contractor as follows:

- an independent contractor could be an individual or a legal person (such as company), whereas an employee can only be an individual, who receives wages as consideration;
- when an independent contractor renders his or its services, this will not be subject to the authority of the beneficiary of said services (i.e. does not have a work schedule) and, in some cases, an independent contractor may own a company or establishment; and
- labour relationships are regulated by the FLL, while independent services are regulated under the civil or commercial codes, as commercial or civil contracts in which consideration is not construed as salary.

b. General Differences in Tax Treatment

Employment Tax Obligations

An employee's salary is subject to income tax ("ISR", is the acronym in Spanish), and an employer is obligated to withhold and pay this tax on the employee's behalf.

Social security dues are considered taxes for legal purposes. As in the case of ISR, an employer is responsible for withholding and paying the employee's dues, as well as for the payment of its own.

Contributions to the National Housing Fund for Workers ("INFONAVIT", for its acronym in Spanish) are also considered taxes. The employer has to pay 5% of the worker's salary to this fund.

The employer is also responsible for the payment of local payroll taxes.

Independent Contractors Tax Treatment

An independent contractor is responsible for paying ISR, however the beneficiary of the services may have to make provisional withholdings from the independent contractor's revenue.

Furthermore, independent services are subject to Value Added Tax (VAT) payment.

c. Differences in Benefit Entitlement

Employee's Benefits

The FLL grants all employees rendering services in Mexico certain fundamental, non-waivable rights. In turn, the employers of such employees have the corresponding statutory obligations to satisfy these rights.

The FLL explicitly sets out that employees are entitled to the following non-waivable fringe benefits:

- a year-end bonus (Christmas Bonus) equivalent to at least 15 days of wages, payable prior to 20 December each year;
- a yearly vacation period, the length of which is dependent on the worker's seniority;
- a vacation premium of 25% of the salary payable to him/her during the vacation period; and
- mandatory paid holidays on January 1, the first Monday of February to commemorate February 5, the third Monday of March to commemorate March 21, as well as May 1, September 16, the third Monday of November to commemorate November 20, December 1 (every six years when a new President is elected), December 25, and any other holidays established by federal or state law.

In addition to the above-described benefits, all employees of a business are entitled to share in 10% of their employer's pre-tax profits, with the exception of the managing director, administrator or chief executive officer (or the equivalent position, regardless of the title given). The chief executive officer has been interpreted by the labour courts to mean the person who has the highest hierarchical position in the business (article 127, paragraph 1, FLL).

In addition, it is mandatory for all employees to be registered in the social security system. The basic services provided by the social security include work hazard, general medical services, maternity, nursery services and retirement pensions.

Employers have to register workers in the INFONAVIT, which is a mandatory benefit.

Independent Contractors

Independent contractors are not entitled to any benefit derived from their civil or commercial contract, other than the consideration agreed therein.

d. Differences in Protection from Termination

Employees

Unlike in other countries, where 'employment-at-will' is the general rule, the FLL protects 'job stability'. An employer in Mexico may only dismiss an employee without liability if there is a cause for the dismissal.

Article 47 of the FLL sets out the specific conduct that constitutes cause for dismissal without liability for the employer, while article 185 of the FLL provides a specific cause for

the dismissal of an employee in a management position, specifically when the employer has reasonable grounds for having lost confidence in the employee. An employer must personally notify the Labour Board in writing, at the time that the incident occurs or within 5 business days, of any specific cause for dismissal as well as of the employee's last registered address, so that the Labour Board can notify the employee in person. If neither is done, the dismissal will be considered unjustified.

The employer's right to dismiss the employee without liability expires 30 days after the date on which the employer becomes aware of the statutory grounds for the dismissal.

In the case of managerial employees, temporary employees, employees with less than one year's service or domestic employees, if an employer does not have any statutory grounds for dismissal, but nonetheless desires to terminate the employment relationship, the employer must make the following severance payment:

- constitutional indemnity equivalent to 3 months of consolidated salary (total compensation that includes the base salary and all the benefits provided to the employee, whether in cash or in kind, in connection with his employment and with no deductions);
- seniority premium consisting of 12 days of salary for each year of service, with a cap of twice the minimum wage; and
- 20 days of consolidated salary for each year of service;
- accrued benefits earned during the last year of service, such as Christmas Bonus, Vacation, Vacation Premium, Savings Fund, Commissions, and Performance Bonus if any, etc.

In the event of litigation, if an employer cannot prove that the causes of termination are justified, then the employee may make a request to the Labour Board for reinstatement to his previous job, or a constitutional indemnification equivalent to 3 months of consolidated salary, and all accrued benefits. The Employee will also have the right to receive unpaid salaries, being the salaries he is owed from the date of termination up to a maximum period of 12 months. If after the 12 month period the trial has not ended or the final resolution has not been complied with, the employee will also be entitled to the payment of interest generated, at a rate of 2% over a 15 month salary basis.

Independent Contractors

Termination of a civil or commercial contract is subject to the covenants included therein, for example an expiration term (or end date), mutual agreement, breach of contract, *force majeure*, acts of god, etc.

e. Local Limitations on Use of Independent Contractors

The FLL foresees the possibility that an established independent contractor provides services with its own employees to another employer, providing that the independent contractor has sufficient assets, economic standing and means to face all the responsibilities towards its own employees and all possible labour contingencies. If this were not the case, the employer receiving the services provided by the independent contractor will have a joint responsibility towards the independent contractor's workers or employees.

According to the FLL, in addition to an independent contractor and employer being jointly responsible, in the event of an independent contractor providing the abovementioned services exclusively to one employer, the independent contractor's employees have to be entitled to the same working conditions provided by the employer receiving the services (article 15, FLL).

f. Other Ramifications of Classification

The FLL provides that an intermediary is an independent contractor (an individual or a legal person) that hires or intervenes in the hiring of other individual or individuals to render their services to an employer. In this case, the intermediary would not be considered an employer.

Subcontracting or seconded employees have an entitlement to legal treatment, to be discussed in the following Section.

g. Leased or Seconded Employees

The FLL, as per the reforms enacted on December 2012, includes Article 15-A, which increases the regulations on leased and seconded employees under the concept of 'outsourcing' with additional strict regulations. Under the FLL, 'outsourcing' will be defined as follows: The subcontracting (*outsourcing*) regime occurs when work is performed or services are rendered by a subcontractor, providing its workers to perform services for a contractor. The services are rendered under the contractor's control, which sets the tasks for the subcontractor and supervises its services.

This type of work must comply with the following conditions:

- it cannot cover all of the activities of the contractor, whether equal or similar in whole, undertaken at the work centre;
- it is justified due to its specialized character; and
- it cannot include tasks equal or similar to the ones carried out by the contractor's workers.

If any or all of these conditions are not met, the contractor will be deemed to be the employer for all purposes and effects under the Law, including as it applies to obligations related to social security.

The FLL also establishes new requirements, including that the contract must be in writing and that the contractor (or beneficiary of the services) shall ensure that the subcontractor complies with its obligations under the labour law. It further provides that the subcontracting regime will not allow the transfer of workers from a contractor to a subcontractor, for purposes of undermining any worker's right provided by the FLL.

The wording of these regulations is ambiguous. Many of these conditions are difficult to determine and impractical in their application. Furthermore, in practice, the proposed outsourcing regulations have a substantial impact on employers, since many of them have a corporate structure depending on service companies to provide specialized functions. In addition, the cost of business also increases for many business groups that have outsourced their entire workforce through service companies, when considering the company's profit-sharing obligations for an entire group of workers, in case that the contractor is deemed to be the employer.

h. Regulations of the Different Categories of Contracts

Employee relationships are regulated under the FLL, which is a public interest law, and therefore its basic principles are non-waivable. Its nature is very protective of workers' rights.

Independent contracts are regulated under the Civil Code or the Commerce Code. These codes are private in nature, as conceived in civil law countries, and consequently the will of the parties shall prevail. The regulations in the codes are of a subsidiary nature.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

It was a very common practice for employers to characterize certain labour relationships as services provided by an independent contractor. The most common were the cases of business promoters, salespersons, traveling salesmen and other individuals engaged in similar activities. In fact, in most of these cases the person rendering the service was really under the authority and subordination of the person receiving the services, since the latter determined the tasks and conditions of the services rendered. Additionally, the 'employer-in-fact' tried to characterize the wages as commissions.

Due to the above, the FLL was amended to address the fact that individuals rendering the services described in the preceding paragraph were in fact workers and not independent contractors when they provided their services personally and on permanent basis.

b. The Legal Consequences of a Re-Characterisation

If the hypothesis described in the previous Section takes place, the person receiving the services will be considered to be the employer and will be liable for the previously withheld legal benefits to the now re-characterized employee.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

If a 'supposedly' independent contractor believes that he/she is in fact an employee in accordance with the FLL, he/she will bring a claim to the Conciliation and Arbitration Labour Boards, to be considered as an employee (mostly in cases of contract termination). The judicial practice is that the Conciliation and Arbitration Labour Board will label the relationship to be one of a 'labour' or employment nature, and the person receiving the services will have the burden of proving the civil or commercial nature of the relationship, which is a rather difficult task.

We quote, below, the criterion of the Supreme Court regarding this subject:

"To determine the legal nature of an agreement we must not only consider its name, but its contents, because, in some cases, contracts named as commission agency agreements are truly employment agreements. Therefore, it is essential to take into account the terms and conditions agreed, in order to conclude if the so-called agent is or is not subordinated to orders given by the principal. We must not forget that according to the Federal Labour Law, subordination is the characteristic element of an employment relationship. Therefore, if analysing the corresponding agreement; i) it is evident that the agent undertakes to sell and promote the products, merchandise and articles handed to him by the principal, as consignment, through the company or third parties, declaring that he has the resources and personnel appropriate to make the sale and promotion (that is, the sale is not necessarily done by the former); ii) it is evident that the agent may be present or absent any time he wishes, because he is not obliged to personally carry out the assignment, iii) that the contract does not confer exclusivity for any of the parties and therefore has full freedom to hire other agents, iv) that he may perform his activity independently (which excludes subordination), and v) it is evident that it is a commission agency agreement, even if it includes clauses regarding deposit of the sales, storing merchandise, shortages, cash cut-offs, inventories and audits, as well as those regarding limitations to hire other agents, then these are not orders, as understood in an employment relationship, but contractual rules that enable an adequate performance of the commission."

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In the event that a re-characterized employee's legal claim before the Labour Boards is successful, the company deemed to be the employer will be responsible for the payment of outstanding and accrued benefits, outstanding salaries; as well as for any outstanding social security and housing contributions due to the INFONAVIT, including tax liabilities for any of these omissions.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Independent contractor relationships should be recorded in writing and specifically describe the commercial or civil nature of the agreement.

If the services are to be provided personally, it should be specified that the contractor will perform under its own authority, not subject to a work schedule or reporting obligations to any representative of the beneficiary of the services. The contractor should use its own resources, for example office space, instruments, devices, tools, etc.

If the services are to be provided by an individual or legal person using its own employees, he or it shall be responsible for complying with all labour obligations, including social security and INFONAVIT. The contractor should also perform the services using its own material and financial resources, and operate under his or its authority.

b. Day-to-Day Management of the Relationship

The person receiving the services shall not give instructions or working orders to the contractor's employees, or provide them with powers of attorney or any kind of representation such as business cards, working instruments, etc. in order to avoid any misconception about subordination between the person receiving the services and the workers of the independent contractor.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Recently, the tax authorities try to characterize all independent contractor agreements where services were rendered by a third party with its own workers, as an outsourcing contract. In doing so, the tax authorities ignored the fact that an outsourcing contract implies the supervision and specification of the tasks to be performed by the employees of the subcontractor, and that there are other contracts that the independent contractor performs with its own workers and not under the supervision of the person receiving the services.

This criterion by the tax authorities has serious implications regarding VAT accreditation when not all the conditions set forth in article 15-A of the FLL are met, resulting in the beneficiary being considered as the employer of the subcontractor's workers. Therefore, the tax authorities deem this contract to be a labour agreement rather than a commercial or civil agreement between the subcontractor and the contractor, as set out in the following Federal Courts decision:

“The Supreme Court of Justice has established binding jurisprudence to the effect that notwithstanding the strict interpretation of tax laws as provided in article 5 of the Federal Fiscal Code, does not preclude other methods to interpret the actual intent of the legislator when its literal analysis leaves to doubt. Consequently, the concept of ‘subordination’ in article 14, last paragraph of the VAT Law that establishes that the rendering of independent services performed by a person in a subordinated condition receiving a remuneration excludes the payment of said tax since it coincides with the definition of a labour relationship as provided in the Federal Labour Law, this leads to the conclusion that in the specific case of determining whether the personnel subcontracting is of labour nature or of independent nature, it will be important to refer to article 15-A of the Labour Law considering that this provision establishes the conditions to determine whether there is an actual subordination of the worker to the contractor, important situation to determine the application of the tax law. Consequently, if not all the requirements provided for in article 15-A are met, the contractor will be considered employer for all legal effects and no VAT will be caused, thus the contractor has no right for its accreditation...”

b. Recent Amendments to the Law

Rules and regulations of the Tax Code for 2017 include amendments to the provisions of the ISR and VAT Laws, which require the contractor to obtain from the subcontractor, certain documents related to the payment of salaries and social security obligations to the latter's employees, in order for the contractor to be able to deduct the ISR or accredit the VAT.

VI. BUSINESS PRESENCE ISSUES

A permanent establishment is a tax fiction, as it does not correspond with a company duly incorporated for legal effects in a country. Instead, it consists of a figure acquiring a variety of tax obligations, whether formally or substantially to comply with tax obligations established by the Mexican legislation. In other words, permanent establishment is the term used for tax effects, as 'branch' commercially speaking.

In this respect, generally, permanent establishments in Mexico are bound to pay ISR (at a rate of 30% over earned profit) applicable to the establishment's attributable income. Consequently, it must comply with the tax obligations applicable to Mexican corporations, such as being registered in the RFC, carrying out company bookkeeping, issuing invoices, which meet specific requirements (electronic and authorized by the tax authorities), among others.

Further on the aforementioned analysis, article 2 of the ISR Law provides the definition of permanent establishment as follows:

“[...] Any place of business in which commercial activities are performed, whether totally or partially, or in which independent personal services are rendered. It shall be understood as permanent establishment, among others, the branches, agencies, offices, factories, workshops, facilities, mines, quarries or any other place of exploration, extraction or exploitation of natural resources.

Notwithstanding the preceding paragraph, when a non-resident acts in the country through a natural or legal person, other than an independent agent, the non-resident will be considered to have a permanent establishment in the country, in relation to all the activities performed by such natural or legal person for the non-resident, even when not having [the non-resident] a place of business for the provision

of services within the national territory, if such person exercises powers to execute contracts in the name or on behalf of the non-resident to conduct its activities in the country, which are not mentioned in article 3 of this Law.”

As can be observed from reading the previous paragraphs, a permanent establishment is a place of business in which commercial activities take place, or in which independent personal services are rendered; or by cases in which the foreign entity acts through an independent agent in the country, to whom it has granted certain powers of attorney.

VII. CONCLUSION

When conducting business in Mexico, it is essential to analyse the legal implications of the correct characterization of the relationship to be established with individuals who will provide or deliver services for the company.

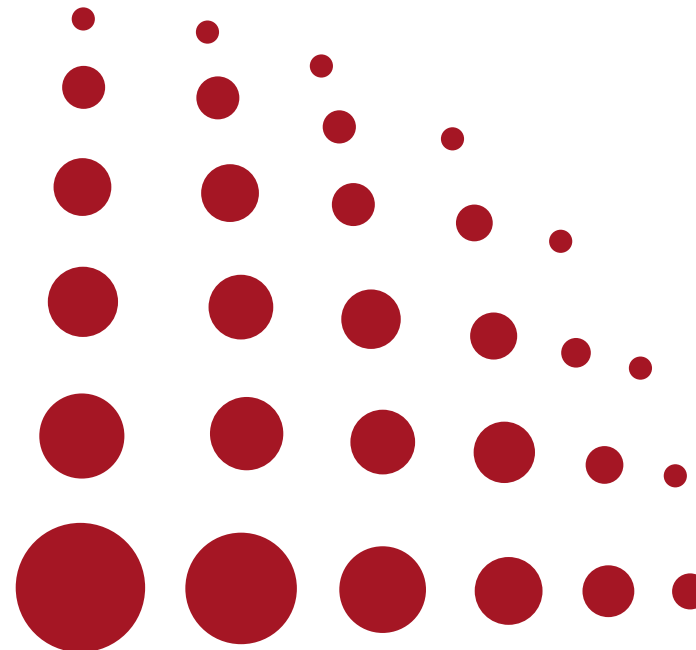
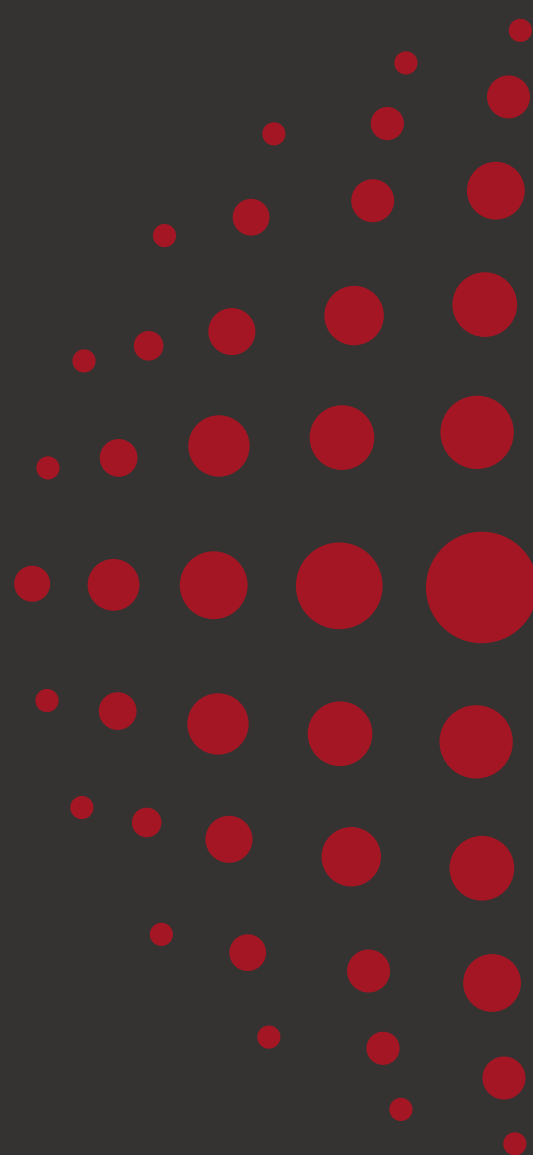
As explained in this article, the laws make a clear distinction between a labour relationship and an independent service contract: labour relationships are regulated by the FLL which is very protective of workers and employees, and imposes unavoidable obligations on an employer, whereas independent service contracts are regulated under civil and commercial laws which allow a wider scope to negotiate the conditions under which the services will be rendered.

It is important to consider the risks involved in trying to disguise a labour relationship as an independent service contract, particularly taking into account the protective nature of the labour laws and the presumption that most of the personal services are labour in nature.

Seeking professional labour legal advice is always recommended in order to ensure that nature of the contract correctly corresponds with the personal services being provided.

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NETHERLANDS

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I. OVERVIEW

a. Introduction

Understanding the distinction between an employee and an independent contractor begins with qualifying the agreement in force between the parties. The parties who enter into an “employment agreement” are an employer and an employee. These parties are not separately defined in the Dutch Civil Code (DCC). The parties who enter into a “contract for services” are known under Dutch law as an (independent) contractor and a principal.

The question whether an agreement between two parties should be qualified as an employment agreement or as a contract for services continues to provide new case law and legal literature. The Supreme Court first ruled that there is not a decisive element for answering this qualification question¹. All the elements characterizing the relationship must be taken into consideration and assessed jointly. None of these elements – which will be discussed later on – have to be decided in advance. According to the Supreme Court, the initial parties’ intention can yield for a future manner of execution. This means that for example, although parties may have labeled the agreement in force between them as an employment agreement, this (title on the agreement) is not necessarily decisive. It can be inferred from the case law from the Supreme Court; the court must first decide on the parties’ intention, as it then must determine, based on the actual manner of execution if - other than the original parties’ intention – the manner in which the agreement is executed, leads to the conclusion that there is a different kind of agreement in force between the parties.

The outcome of the qualification question is important for several reasons. One of them being: if the labour relationship is qualified as an employment relationship (eventually in court), the employer is/was responsible to withhold income taxes as well as the workers’ income contributions.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The Dutch Civil Code lays down three forms of contracts relating to the performance of work. Where work is performed for valuable consideration the legal relationship between the parties will fall into one of these categories:

- employment agreement;
- contract for services;
- contract of work.

A contract of work (agreement) is defined as an agreement whereby one party as an independent contractor agrees to produce particular work of a tangible nature for a sum of money to be paid by the other party. There is no master and servant relationship between the contractor and the other party and there is no obligation for the contractor to perform his duties personally. In practice, it is generally relatively straightforward to distinguish a contract for work agreement.

This chapter will discuss the elements, which should be taken into account to determine whether an agreement between parties should be qualified as an employment agreement or as a contract for services. The answer to this question will lead to the qualification of the worker, being an employee or an independent contractor.

¹ in the so-called Groen/Schoevers judgment.

Employment agreement

An employment contract is defined by the Dutch law: “Parties have entered into an employment agreement (relationship) when one party, an employee, commits himself to perform labor in the service of the other party, the employer, against remuneration during a certain period of time.”

Three core elements must be present in order for an employment agreement to exist under Dutch civil law:

- the employer is entitled to give orders as to how the work is to be carried out (*relationship of authority*). What is determinative is if the employer is entitled to give orders, not if he actually does.
- the work is to be carried out *personally* (exclusively) by the worker, and
- the worker receives *remuneration* (wages) for his work from the employer.

Substance over form

As stated in the introduction, the parties' intentions and the way they have given actual effect to the agreement, are relevant elements in deciding whether or not there is an employment agreement. If the situation meets the three core criteria, then, notwithstanding any arrangement, which the parties have agreed upon to the contrary, the contract may be classified as an employment contract (substance over form) and an employment agreement is deemed to exist. Factual elements to take into consideration are discussed further on in this chapter.

Legal presumption

If, for at least three consecutive months, work is performed for remuneration either for at least 20 hours per month or on a weekly basis, it is presumed that this work is performed under an employment agreement. This presumption of law is important in situations where it is unclear whether there is an employment agreement, either because no clear contract was reached or because the course of actual events differs from the agreements made in the contract. This legal presumption can be rebutted by evidence to the contrary.

Categories of employees

Employees can be employed on different types of contracts, namely:

- indefinite term;
- fixed-term;
- temporary (agency).

Contract for services

A contract for services is defined by the Dutch law. There is a contract for services when activities are conducted that consist of anything other than the creation of a work of material nature, the retention of property, publishing works or the carriage or transportation of persons or property.

The independent contractor is contracted on the basis of a contract for services or a management agreement, which is a specific form of a contract for services. These contracts can be entered into with a natural person or the individual person's management company (Service Company).

Instruction right but no relationship of authority

The existence of an instruction right is not decisive in qualifying the agreement. Following the law, the independent contractor is obliged to give effect to timely and responsible instructions provided by the principal regarding the performance of the services. This instruction right is however, not comparable to the relationship of authority between an

employee and an employer.

Circumstances to take into consideration

So which circumstances (elements) in addition to any instruction right of the (potential) employer are relevant to determine whether a worker can be qualified as an employee or as an independent worker? Relevant circumstances include, but are not limited to:

- the freedom of the worker regarding the organization of his work;
- the nature of the remuneration;
- whether payments are made directly by several clients;
- the extent to which the worker bears an entrepreneurial risk;
- the extent to which the worker supplies his/her own raw materials and consumables and tools;
- whether there is continued payment during vacation time, illness and leave;
- the extent to which, in addition to the agreed work, other work is performed;
- the occasional nature of the work;
- any deduction of social security contributions and payroll taxes by the (potential) employer and any payment of VAT by the worker.

b. General Differences in Tax and Social Security Laws

If an employment agreement is held to exist from an employment law perspective, it will be an employment agreement from a social security and tax law perspective. From a social security and tax law point of view, however, some working relationships are considered to be employment relationships, even though they do not meet all requirements of the Dutch Civil Code. However, as soon as the supposed employee can prove that he/she is, in fact, a self-employed worker, this presumption will be rebutted.

If there is an employment agreement, payroll taxes must be withheld and paid. The Income Tax Act 2000 and the Salaries Tax Act 1964 do not contain a definition of what constitutes an employment agreement. The tax laws are in line with the private criteria as stated under the subject 'employment agreement'.

The employer is responsible to determine whether the labour relationship qualifies as an employment relationship for tax and employed persons' income contributions ('social premiums'). If the labour relationship is qualified as an employment relationship (eventually in court), then the employer is/was responsible to withhold income taxes as well as the worker's income contributions.

Tax and social security authorities have developed guidelines containing criteria by which it is to be determined whether the worker is performing his activities as an employee (Dutch Civil Code), an employee for tax and social security reasons or as an independent contractor. Relevant circumstances include the number of expected assignments. Assessment of Employment Relationships (Deregulation) Act

Until May 1st 2016, an independent contractor could request the Dutch Tax Authorities to issue a 'Declaration of Independent Contractor Status' (in Dutch: "Verklaring Arbeidsrelatie" or "VAR"), which enabled the independent contractor to make a reasonable case for self-employed status to his principal. With this declaration, the principal was indemnified against claims of the Dutch Tax Authorities (wage tax levy).

However, as of May 1st 2016, the Assessment of Employment Relationships (Deregulation) Act (in Dutch: "Wet Deregulerend Beoordeling Arbeidsrelaties" or "Wet DBA") entered into force as a result of which the 'Declaration of Independent Contractor Status' is abolished. Further to that, principals are no longer indemnified against possible claims of the Dutch Tax Authorities. In addition, new assignments for independent contractors

must be contracted in compliance with this new act.

In order to exclude risks in advance and to be sure about the work relationship between the independent contractor and the company, it is important to ensure there is no possibility of any employment relationship between the parties and that the contractor is not working under any form of authority. In order to facilitate this, the Dutch Tax Authority published several 'model agreements', which may be used. Please note that there is a lot of discussion about the quality of these 'model agreements'.

Initially, an implementation phase of one year applied. However, because of a lot of concerns regarding this new act, the minister extended the implementation phase to – in any case – January 1st 2018. Until this date, a reticent enforcement policy applies and the Tax Authorities will assist organizations with the implementation unless the company is 'evidently malicious'. In the latter case, the Tax Authorities will immediately impose fines and/or an additional tax assessment.

c. Differences in Benefit Entitlement

The most important differences in benefit entitlements and other rights and obligations between an employee and an independent contractor are stated below.

In 2017, the contribution rates are as follows:

EMPLOYEE	INDEPENDENT CONTRACTOR
<ul style="list-style-type: none"> Unemployment benefits Entitlement to 70% of salary during the first two years of illness Holiday, holiday pay and leave entitlement Minimum wage Pension scheme Non-competition & confidentiality clause Unfair dismissal protection Health, safety and working hours Equal treatment 	<ul style="list-style-type: none"> Not applicable Not applicable Not applicable Minimum wage Not applicable Non-competition & confidentiality clause Not applicable Health, safety and working hours Equal treatment

d. Differences in Protection from Termination

General

Dutch law gives *employees* fairly extensive job security. Once entered into, an employment agreement can only be terminated unilaterally if certain conditions are met and certain formalities complied with.

Although the rules are rather restrictive, it is not the intention of the Dutch labour law to impose unreasonable restrictions on the employer where dismissals are justified.

The protection from, and the conditions under which unilateral termination of an employment agreement is possible under Dutch civil law, do not apply for independent contractors.

Employment agreement for a definite period

It is possible to enter into an employment contract, which terminates without having to

comply with any particular formalities simply by fixing the term of the agreement for a definite period. The agreement will then terminate automatically at the end of the fixed period of time.

Notification obligation

One month before the termination of a fixed-term employment contract of six months or longer, an employer must notify the employee whether the employment contract will be extended or not (in Dutch: *aanzegverplichting*). If so, the employer must also inform the employee about the terms and conditions for extension. If the employer does not inform the employee, the employee has a right to claim salary during the period in which the employer is in violation (up to a maximum of one monthly salary).

For fixed-term employment contracts shorter than six months or contracts with no fixed end date, such as for the length of a specific project, this notification is not required.

Employment for an indefinite period

If no specific period is mentioned, or the agreements exceed the legally permitted period or number of consecutive contracts, an employment contract will be deemed to be a contract for an indefinite period of time. This employment agreement will not terminate automatically.

Consent of Employee Insurance Agency ('UWV')

In case of dismissal on economic grounds or because of long-term incapacity of work, an employer can terminate an employment contract by giving notice after the Employee Insurance Agency has given permission to do so by granting a dismissal permit. The Employee Insurance Agency will only grant permission if there is a reasonable ground for dismissal and redeployment within a reasonable period of time is not possible (even after training) or reasonable. After permission has been granted, notice is to be given with due observance of the notice period. Due to the time involved in obtaining permission from the Employee Insurance Agency, the employer can deduct the duration of the procedure from the notice period (provided that at least one month of notice remains).

Since July 1st 2015, there is a possibility of appeal against a decision of the Employee Insurance Agency.

Notice periods

Minimum notice periods must be observed in terminating an employment agreement.

Dismissal without UWV consent

Termination of an employment agreement without the approval of the UWV is null and void, unless the termination:

- is by mutual consent; or
- is for urgent reasons; or
- has been decided on by a Court; or
- occurs during the 'trial period'; or
- is of a fixed-term agreement; or
- is in respect of the employment of a managing director as defined in the company's articles of association.

Termination by Court proceedings

A judge can terminate an employment contract in case a reasonable ground for dismissal exists and redeployment within a reasonable period of time is not possible (even after training) or reasonable. An employment contract can be terminated by court decision by filing a petition for dissolution in case of:

- frequent and disruptive absence due to illness;
- unsuitability for the position / underperformance (other than because of illness);
- culpable acts or omissions of the employee;
- refusal to work due to a serious conscientious objection;
- impaired working relationship as a result of which the employer cannot reasonably be required to continue the working relationship;
- other reasons and/or circumstances (by way of an exception).

Since July 1st 2015, there is a possibility of appeal against a court's decision.

The statutory transition payment

Until July 1st 2015, Dutch employment law did not provide a statutory severance payment. Until that date the Dutch courts generally applied the 'Cantonal Court Formula'. This formula was also often used to calculate the severance payment in case of termination of the employment contract by mutual consent.

As from July 1st 2015, a statutory transition payment (in Dutch: *transitievergoeding*) is introduced. Every employee is entitled to this payment when an employment contract has lasted at least 24 months and is terminated on initiative of the employer or by operation of law, subject to a few exceptions (including dismissal for urgent cause).

When calculating the amount of the statutory transitional payment, only the length of employment will be taken into consideration. For calculating the duration of an employment contract one or more employment contracts between the same parties (or successors) that have followed each other with intervals lasting no longer than six months will be counted together.

The transition payment is 1/6th of a monthly salary for every half year for the first 10 years of service and 1/4th of a monthly salary for all years of service above 10 years. The transition payment is capped at EUR 77,000 as per January 1st 2017 or - if the employee is entitled to a higher annual salary - one annual salary.

The transitional payment is not due in case the employee terminates the employment contract, unless this termination is a result of seriously culpable actions on behalf of the employer.

Fair dismissal payment

In addition to the statutory transitional payment, the court may also award a fair dismissal payment, however, only in case of seriously culpable acts and omissions on the part of the employer. This only applies to exceptional situations.

Exceptions to the entitlement of the transitional payment

There are a number of exceptions regarding transition payment, the most important of which are set out below. Until January 1st 2020, employees over the age of 50 with an employment contract lasting at least ten years must be paid a transition payment of 1/2th of their monthly salary for every six months that the employment contract with the employer has continued after reaching the age of 50. This does not apply if the employer had less than 25 employees in the second half of the calendar year preceding the calendar year in which the employment is terminated.

In case of 'small' employers who employed fewer than 25 employees on average in the second half of the calendar year previous to the calendar year in which the employment contract was terminated because redundancies were necessary by economic circumstances resulting from the employer's poor financial situation, it will only be necessary to take the duration of the employment from May 1st 2013 into account when calculating the transition payment. The years of service prior to this date will not be

taken into account. This exceptional arrangement will continue until January 1st 2020. Please note that it will not be easy to qualify for a poor financial situation within the meaning of this arrangement.

The statutory transitional payment will not be owed if the employee is younger than 18 and the average working hours did not exceed 12 hours per week. The transitional payment will also not be owed if the employee's employment contract ends because of reaching the pensionable age or another age at which the employee is entitled to a pension. Furthermore, transitional payment will not be owed if the employment is terminated or not continued as a result of a grave culpable act or omission on the part of the employee. In the latter case, the cantonal court may also grant the transitional payment in part or in whole in case no payment at all would be unacceptable according to the criteria of reasonableness and fairness.

Contract for services

As stated, the protection from, and the conditions under which unilateral termination of an employment agreement is possible under Dutch civil law, do not apply for independent contractors. As an employment agreement, a contract for services can be concluded for a definite or for an indefinite period. The contract for services should include an earlier termination clause as well as a reasonable notice period, because an independent contractor can otherwise be entitled to a severance pay. If these criteria are met, a principal can easily terminate the contract for services by giving notice while observing the applicable notice period.

e. Local Limitations on Use of Independent Contractors

There are no limitations on the use of independent contractors under Dutch Law.

f. Leased or Seconded Employees

If a business does not want to hire (more) employees and does not want to come to a contract for services either, there are several possibilities under Dutch Law to attract workers. This chapter discusses temporary/agency workers, so-called 'pay rolling' and secondment.

Temporary/agency workers

An agreement under which an employee is supplied to a third party (the recipient), by the employer (the supplier), in the practice of the profession or operation of business of that employer, to carry out the third party's work under the third party's management and supervision in accordance with the orders/instructions given to the employer/supplier by the third party, will be held to be an employment agreement between the supplier ('*uitlener*') and the temporary worker ('*uitzendkracht*'). Temporary employment agencies, placement agencies and labour pools fall within this definition.

All standard labour law provisions apply to this temporary employment agreement, (although exceptions apply in relation to consecutive fixed-term agreements). Other terms can be laid down by collective bargaining agreement and there is a collective bargaining agreement for temporary workers. The provisions of this collective bargaining agreement have been declared generally binding by the Minister of Social Affairs and Employment.

The recipient of the temporary services is liable for all damage suffered by temporary workers during the performance of their duties. Temporary workers who have been working for the recipient for 24 months or more, count towards the recipient's group of regular employees, adding to the number of staff required to establish a works council.

‘Payrolling’

Payrolling makes a distinction between the material and the formal employer. The payroll company is the employer by paper, but the principal is the employer, which exercises the authority over the employee. Payrolling can vary from outsourcing the payroll administration and formal employership, to transferring all existing employment contracts to the payroll company. Distinguishing formal and material employership may lead to a discussion of which party has a certain obligation towards the employee. For instance reintegration obligation when the employee is sick.

The collective bargaining agreement for payrolling states payrolling, consists of a triangular relationship where the principal recruits and selects the employee. The employee then enters into an employment contract with the payroll company, to then be exclusively available to the principal.

The legal status of payrolling is unclear. Payroll companies usually see themselves as a (special) temporary employment agency. In a temporary employment agreement there is also a triangular relationship where the employee, in the context of the exercise of the profession or business, is made available to carry out under the supervision and guidance of a third. There are however important differences between the two. The first one being that with payrolling, the workers are being recruited and selected by the principal, while with a temporary employment agreement the temporary employment agency recruits and selects the workers. Therefore, it can be stated that the payroll company does not have an allocation function, namely bringing supply and demand of temporary work together. However, please note that the Dutch Supreme Court judged in April 2016 that it is no longer required for a company to have an ‘allocation function’, in order to fall under the definition of ‘an employment agreement between the supplier (*‘uitlener’*) and the temporary worker (*‘uitzendkracht’*)’. As a result of this judgment, a lot of employment law triangular relationships, such as payrolling, will fall under the scope of the specific laws for temporary employment agencies.

The employers’ desire for a payroll construction does not have to do with needing more employees in situations of high work pressure or sickness. It stems from the desire to mitigate administrative and labour costs, obligations and liabilities and increase the flexible use of manpower. Usually, not a temporary but a permanent provision is intended. Another related issue of difference between payrolling and temporary employment agreements is that with payrolling there is in general exclusivity: without the consent of the principal, the payroll company is not allowed to redeploy ‘its’ employees.

Increasingly not only newly recruited staff are employed by a payroll company, but also existing contracts of the employer are acquired by a payroll company. Payrolling is relatively common in the primary sector, especially agriculture. In other parts of the business, payrolling is also established, ranging from the cleaning sector, catering, retail and education. Payrolling is (partly due to the mentioned increase) increasingly criticized due to the fact it is sometimes unclear to the employee who is indeed his employer and therefore to whom he can turn in case of a claim. It is also relatively simple for the principle to terminate the contract for services with the payroll company. The payroll company then has to obtain permission of the UWV to terminate the employment agreement with the employee. The risk of using a payroll construction to evade permanent employment contracts, has been discussed in parliament several times. Legislative proposals have been announced in order to counteract this.

The Act allocation of labour through intermediaries (‘WAADI’) already states that workers who are supplied by a third party (which may include payrolling) should be rewarded in the same manner as comparable workers. This also applies to inter alia working hours, overtime, breaks, rest periods, night work, and holidays.

Secondment

Employers who do not provide intermediate services on the labour market or only occasionally supply manpower services to fellow employers do not fall into the category of ‘employer/supplier’. The most important difference is that the specific provisions for suppliers and temporary workers, as set out above, do not apply to such secondments.

An employee who is seconded to a third party to perform his job under that party’s management and supervision, in accordance with the orders given by that third party, will remain employed by his employer. The conditions under which the employee is employed will remain the same and must be adhered to by the third party. A secondment will usually be for a fixed period or for the duration of a specific project.

It is advisable for the employer and the third party to set out the conditions of secondment in an agreement which should specify the terms on which the secondment will take place, including any terms in relation to indemnities, confidentiality, non-solicitation, notice periods and the method of payment for the services rendered.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

The employment contract has been defined in Article 7:610 of the Dutch Civil Code and the contract for services has been defined in Article 7:400 of the Dutch Civil Code. The legal criteria and guiding principles on the basis of which the type of contract is determined have been explained above in part one.

b. The Legal Consequences of a Re-Characterisation

If a labour relationship is qualified as an employment contract, the employee is protected by Dutch employment law, e.g. regarding minimum wages, holidays, sickness, termination, pensions rights, collective bargaining agreement. Please see part one for a short overview of the most important differences in benefit entitlements and other rights and obligations between an employee and an independent contractor.

Furthermore, the employer will be responsible for withholding income tax and national insurance contributions from the employee’s salaries. The Tax Authorities can claim payment of income tax and national insurance contributions due by the employee from the employer.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

If a person is of the opinion that his or her labour relationship meets the criteria for an employment relationship, this person could request a declaratory decision from the courts about the qualification of the employment contract.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The employer may be confronted with employee benefits in arrears such as outstanding holiday payments, salary entitlements during sickness and/or pension entitlements. The employer could also be imposed fines by the Tax Authorities for not complying with the obligation to withhold income tax and national insurance contributions.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

In order to prevent a relationship of authority – which is one of the key elements of an employment relationship – it is common that a contract for services explicitly includes the independent contractor shall be at liberty to carry out his/her duties to perform the services at his/her own discretion. This also means the specific days and hours on which the independent contractor will perform the services on a weekly basis. However, it is possible to agree to a limitation (maximum number) of hours per week in which the independent contractor will perform the services.

No exclusivity

Seeing as the independent contractor should be entitled to perform professional services for other companies as well, exclusivity in respect of labour is also a key element of an employment relationship. Therefore, it is advisable the independent contractor performs professional services for other companies at the same time. This should also be included in the consideration of the contract for services as an assumption based on which the contract for services was entered into by the principal.

The employer's perspective

If the relationship between parties does not meet the requirements for self-employment, the employer/principal may be faced with claims for tax and social security contributions (under the "pay-as-you-team" system, by which an employer must deduct income tax and social security contributions from an employee's wages or salary and must pay this to the government once a month), and may also have to pay fines and, possibly, damages and compensation for termination of the agreement. Since almost all payments made under such claims cannot subsequently be recovered from the former employee, it is advisable for the employer/principal to make provisions for social security contributions for which he might be/become liable.

V. TRENDS AND SPECIFIC CASES

In recent years, the trend in The Netherlands, much like in other countries, has moved towards an increased use of independent contractors and short-term contracts, making the independent contractors a growing and increasingly more important group in the Dutch employment market.

Due to the economic crisis a lot of redundant employees are let go only to start (continue) working for their previous employer as an independent contractor. Therefore, they lose many of the rights and protections they had as an employee, while often doing the same work as before. Some have argued in legal literature there is – or there should be – a distinction between these so-called 'dependent contractors' versus the independent contractors, who are less dependent on one particular principal and have a better labor market position.

In response to the increase of independent contractors, the Dutch legislature has determined (mid-2012) that independent contractors are entitled to the same level of protection for health and safety at work as employees. The aim is to prevent the independent contractors and employees from competing with each other. To further strengthen the position of independent contractors and remove unnecessary barriers, the legislature has also taken several other measures. Among other things, the government passed a law on 1 April 2013 to give smaller businesses – including independent contractors – a better chance for procurement. The government has also taken measures to reduce the administrative burden for independent contractors.

New developments

Further to the implementation of the the Assessment of Employment Relationships (Deregulation) Act as of May 1st 2016 – as set out in paragraph IIb – there is (for the first time in years) a decrease in the use of independent contractors in the Netherlands. This new act creates uncertainty for contractors and principals about the legal status of their working relationship (contract for services or an employment agreement) and the (possible) financial consequences, which explains the decrease of the use of independent contractors at the moment.

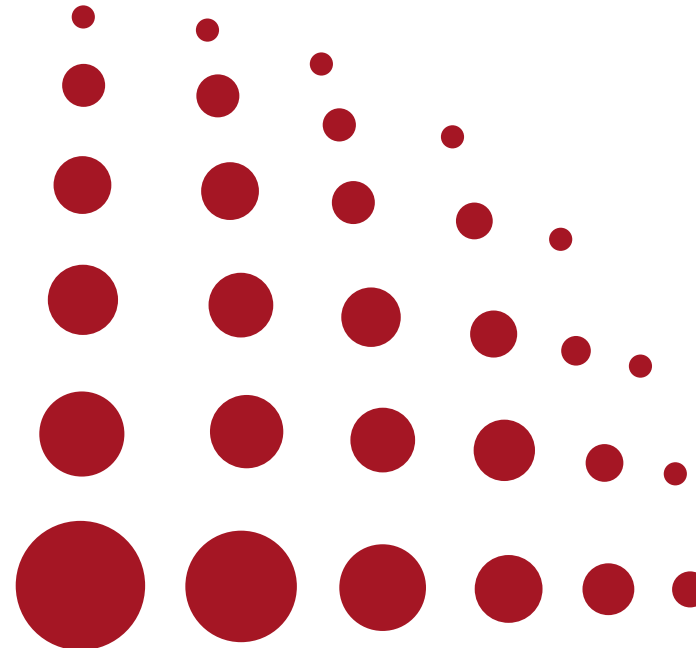
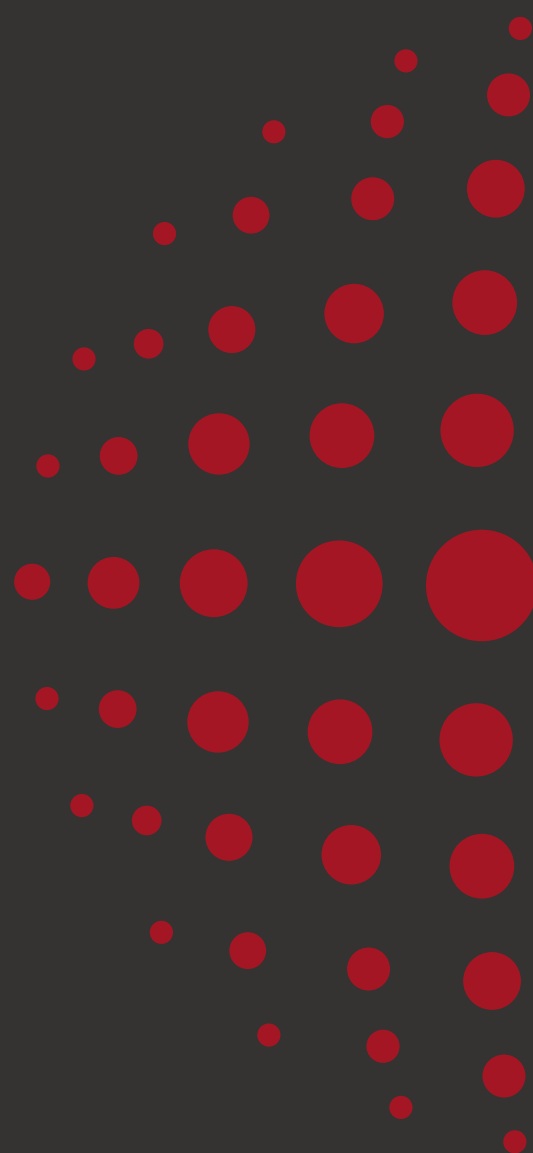
VI. CONCLUSION

The foregoing summarizes some of the distinctions between an employee and an independent contractor under Dutch employment law. Understanding the distinction between an employee and an independent contractor begins with qualifying the agreement in force between the parties. There is not a decisive element for answering this qualification question. All the elements characterizing the relationship must be taken into consideration and assessed jointly. A few elements which have proven to be of importance in case law are the freedom of the worker, the nature of the remuneration and payment during vacation time, illness and leave.

It is important to realize, the initial parties' intention can yield for a future manner of execution. The court must first decide on the parties' intention, as it then must determine, based on the actual manner of execution if - other than the original parties' intention – the manner in which the agreement is executed, leads to the conclusion that there is a different kind of agreement in force between the parties.

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NEW ZEALAND

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I. OVERVIEW

a. Introduction

In New Zealand, the rights and responsibilities of employees and contractors are very different. An employee is someone who is employed to do work for reward under a contract for services (an employment agreement) and a contractor performs services under a contract for services (an independent contractor agreement).

Health and safety laws in New Zealand apply to both employees and contractors, but there are many differences. Employees have all the minimum employment rights under the Employment Relations Act 2000, the Minimum Wage Act 1983 and the Holidays Act 2003 as well as the right to take a personal grievance. Contractors on the other hand are self-employed and usually earn an income by invoicing for their services. They have to pay their own tax, aren't covered by most employment related laws. They do not have the right to bring a personal grievance.

This article focuses on the legal framework for differentiating employees from independent contractors, the re-characterization of the relationship and how to structure an independent contractor relationship.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

New Zealand's Employment Relations Act 2000 (the "Act") applies to all employees, and is predicated on "good faith" in all aspects of the employment relationship. This obligation requires the parties to an employment relationship to be "active and constructive" in establishing and maintaining a productive employment relationship in which the parties are, amongst other things, "responsive and communicative"¹. The Act is intended to promote observance in New Zealand of various International Labour Organisation Conventions. The Act therefore follows a relatively protectionist approach with respect to those engaged as employees.

In contrast, no such statutory requirements of good faith or mutual trust and confidence apply to any contractual relationship in the nature of independent contracting. In essence, a contractor is subject only to the general law of contract. Importantly, a contractor is not entitled to use the mechanisms for resolving personal grievances prescribed in the Act. This article considers the differences between contractors and employees in New Zealand and the process whereby such a relationship can be re-characterised.

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The Act deals with the meaning of the term 'employee'. Section 6 prescribes a requirement for the Employment Relations Authority when deciding whether a person is employed by another person under a contract of service to determine "the real nature of the relationship" between the parties.

Previously, under the Employment Contracts Act 1991, the New Zealand courts had placed heavy emphasis on the terms of the written contract between the parties and had tended to frame the question as "is the person who has engaged himself to perform these services performing them as a person in business on his own account?"²

¹ Section 4 Employment Relations Act 2000 (NZ).

² TNT Worldwide Express (NZ) Limited v Cunningham [1993] 3 NZLR 681 (CA).

Section 6 of the Act provides the definition of an “employee”, and states:

6 “Meaning of employee

(1) In this Act, unless the context otherwise requires, **employee**—

- (a) means any person of any age employed by an employer to do any work for hire or reward under a contract of service; and
- (b) includes—
 - (i) a homemaker; or
 - (ii) a person intending to work; but
- (c) excludes a volunteer who—
 - (i) does not expect to be rewarded for work to be performed as a volunteer; and
 - (ii) receives no reward for work performed as a volunteer; and
- (d) excludes, in relation to a film production, any of the following persons:
 - (i) a person engaged in film production work as an actor, voice-over actor, stand-in, body double, stunt performer, extra, singer, musician, dancer, or entertainer;
 - (ii) a person engaged in film production work in any other capacity.

(1A) However, subsection (1)(d) does not apply if the person is a party to, or covered by, a written employment agreement that provides that the person is an employee.

(2) In deciding for the purposes of subsection (1)(a) whether a person is employed by another person under a contract of service, the court or the Authority (as the case may be) must determine the real nature of the relationship between them.

(3) For the purposes of subsection (2), the court or the Authority—

- (a) must consider all relevant matters, including any matters that indicate the intention of the persons; and
- (b) is not to treat as a determining matter any statement by the persons that describes the nature of their relationship.”

Accordingly, the main consideration under section 6(2), when determining whether a person should be treated as an employee, is the real nature of the working relationship between the parties, rather than the “label” given by the parties to it.³ That is made plain by section 6(3) which states that the authority is not to treat as a determining matter any statement by the parties describing the nature of their relationship, i.e. whether they have said that the relationship is that of principal and an independent contract or employer and employee.

However, at the same time, section 6(3)(a) provides that in making its determination, the authority must consider “all relevant matters” including any matters indicating “the intention of the parties”. As any written contract between the parties at least purports to record their common intention, this requires in every case, an assessment of what the parties have in fact set out in their agreement.

³ *Koia v Carlyon Holdings Limited* [2001] ERNZ 585 (CA).

The authoritative decision on the application of section 6 is the decision of the Supreme Court in *Bryson v Three Foot Six Limited*⁴. In that decision, the Court stated:⁵

“All relevant matters” in s 6(3)(a) ERA certainly include the written and oral terms of the contract between the parties, which would usually contain indications of their common intention concerning the status of their relationship. They will also include any divergences from or supplementation of those terms and conditions which are apparent in the way in which the relationship had operated in practice. It was important that the Court or the Authority should consider the way in which the parties have actually behaved in implementing their contract. How their relationship operates in practice is crucial to a determination of its real nature. “All relevant matters” equally, clearly requires the Court or the authority to have regard to the common law tests.”

In that passage the Court referred to the application of the “common law tests”. *Bryson and Koia v Carlyon Holdings Limited*⁶ are authority for the proposition that, in addition to considering the intention of the parties, the real nature of the relationship can be ascertained by applying the common law tests of:

- control;
- integration; and
- the fundamental test of whether the person performing the services is doing so on their own account.

Bryson and Koia have made it clear that none of these tests can be considered decisive in its own right and the circumstances and facts of each case must be considered as a whole in determining the real nature of the relationship between the parties. However, despite the apparent relegation of the written terms of the agreement to only one of many “relevant factors” to be evaluated, it still has considerable importance. *Bryson* reconciled section 6 with the need to consider the terms of the agreement this way:⁷

“It is not until the Court or authority has examined the terms and conditions of the contract, and the way in which it actually operated in practice, that it will usually be possible to examine the relationship in light of the control, integration and fundamental tests. Hence the importance, stressed in TNT, of analyzing the contractual rights and obligations.”

Accordingly, in the normal course of events, the authority will undertake an assessment of each of these tests, together with the terms of the written agreement, in forming its conclusion on the issue and will adopt a balancing of those matters in order to determine the question. Plainly, cases under section 6 are heavily fact specific.

Therefore, while statements of principle such as those outlined above assist determination of status, the intensely factual nature of cases means that trends in this area are difficult to determine.

Intention of the Parties

In assessing the intention of the parties, the authority will normally take into account some or all of the following factors:

- whether there is any written contract or statements specifically describing the nature of the relationship and containing indications of the parties’ common intentions;
- whether there have been any divergences from those terms and conditions in practice;

⁴ [2005] 3 NZLR 721.

⁵ Above n4 at [32].

⁶ [2001] ERNZ 585.

⁷ Above n4 at [32].

- whether there is any evidence of any relevant discussions or oral exchanges, conduct or correspondence;
- whether the parties have always acted consistently so as to indicate one relationship rather than the other.⁸

The starting point for determining the parties' intentions is the written terms of the agreement between the parties.

As stated by the Act, the intention of the parties is relevant, but is not a decisive factor. However, the Employment Court⁹ stated:¹⁰

"It is a very serious matter for the Authority or the Court to find, notwithstanding the clear intention of highly capable and knowledgeable persons who have equal contracting strength and sound reasons for the arrangements they have mutually entered into, that, after those arrangements have been terminated, the real nature of their relationship was completely different."

Further, intention may be decisive where all other factors are evenly balanced. In the Court of Appeal's decision in Bryson¹¹ (in a passage which was not disturbed on appeal), the judge stated:¹²

"The Act's emphasis on the real nature of the relationship requires that, in cases where the real nature of the work as constituted by the agreement's substantive terms and its objective features point clearly to an employment relationship, there will be little scope for the parties to agree that the relationship is nonetheless a contract for services. In cases where the real nature of the relationship is less certain, the parties will have greater freedom to constitute their relationship in either way."

Control Test

The degree of control a principal/employer has over the contractor/employee is an indication of the true nature of the relationship. Historically, the test looked at whether the employee worker was subject to the over-arching control and direction of the principal party in assessing whether a person was an employee or a contractor.

However, the importance of the control test has been diminished for some time in New Zealand. In TNT the Court of Appeal emphasized the terms of the written employment agreement between the parties and rejected the notion that the degree of control exercised by the alleged "employer" was a decisive factor in determining the true nature of the contract. It stated that while the Employment Court was correct to attach weight to the control test, it could no longer be regarded as the sole determining factor, and could not be decisive.

Despite these statements, the control test has some remaining relevance as made clear by the Supreme Court in Bryson. Then the Employment Court¹³, in assessing the control test, asked various questions of the person's role including:

- whether the individual was left to his own devices;
- whether the individual had a degree of autonomy; and
- whether he could come and go from the alleged employer's premises as he pleased.

⁸ Brookers, *Employment Law in New Zealand*, Wellington, Brookers, 2000.

⁹ *Chief of Defence Force v Ross-Taylor* [2010] NZ EmpC 22.

¹⁰ Above n9 at [30].

¹¹ [2004] 2 ERNZ 526 (CA).

¹² Above n11 at [23].

¹³ *Clark v Northland Hunt* (2006) Inc.

Integration Test

This test considers whether the work performed by the alleged employee is an integral part of the business and whether he or she has effectively become "part and parcel of the organization". The test has become inter-mingled with the "economic reality" test¹⁴, when it was stated:

"The issue that must be settled in today's cases is whether the worker is genuinely in business on his own account or whether he is "part and parcel of" – or "integrated into" – the enterprise that the person or organization for whom work is performed."

In Clark it was stated by Judge Perkins that in a situation with only a single employee/contractor, the integration test is not all that suitable as a measure to be applied.¹⁵

Accordingly, the focus of the test is the extent to which the person is, in all respects, an integral part of the organization for which he or she works. Factors to be considered in determining this question include:

- is the person performing a role that is part and parcel of the organization?
- is the person paid a set fee or payment by results?
- does the person use their own equipment and tools in undertaking the tasks?

Fundamental Test

This test has been variously described over the years as the "fundamental test", the "economic reality test", and the "business test". The test asks whether the person is in business on their own account. The authoritative formulation of the test was brought by jurisprudence¹⁶:

"Is the person who has engaged himself to perform the services performing them as a person in business on his own account? If the answer to that question is 'yes', then the contract is a contract for services. If the answer is 'no', then the contract is a contract of service."

The test has been similarly stated by the Employment Court in another case¹⁷ where the judge stated:

"This test examines whether the person performing the services is doing so as a person in business on his or her own account".

A few years later, the Employment Court considered¹⁸, in attempting to collect the relevant strands of the particular case together:

- what were the payment and taxation arrangements?;
- was the individual registered for goods and services tax?;
- was it a non-exclusive relationship?;
- did the individual have a separate business account?; and
- was the individual able to increase his profits by his own efforts?

Ultimately, the fundamental test is where the Authority collects the evidence together regarding the assessments that it has made in applying the other relevant tests. The Authority attempts to resolve any conflicts in the evidence and forms its view of what the "real nature of the relationship" between the relevant parties is in accordance with section 6 of the Act.

¹⁴ as in *Challenge Realty Ltd v Commissioner of Inland Revenue* [1990] 3 NZLR 42 (CA).

¹⁵ Above n13 at 46.

¹⁶ *Market Investigations Ltd v Minister of Social Security* [1969] 2 QB 173.

¹⁷ *Curlew v Harvey Norman Stores (NZ) Pty Limited* [2000] 1 ERNZ 114 (EC).

¹⁸ *Downey v New Zealand Greyhound Racing Association Inc* (2006) 3 NZELR 501 (EC).

b. General Differences in Tax Treatment

There are fundamental differences in tax treatment for individuals characterised as employees or independent contractors. Although arguably this treatment stems from the way the parties have described that relationship and ought not to be given significant weight in describing the true nature of it. In determining whether a person is an employee under the section 6 test, the New Zealand courts have confirmed that the taxation position is not a neutral factor¹⁹. The Employment Court²⁰ found that payment of withholding tax was not a neutral factor when determining the existence of an employment agreement, but rather indicated against a contract of service. In the same way, invoicing of services to a principal and payment of Goods and Services Tax on those invoices is also not a neutral factor and indicates against a contract of service.

In terms of treatment, every employee is required to pay income tax in the form of PAYE tax ("Pay As You Earn"). PAYE taxes are progressive and the rates at which the various taxes apply are as follows:²¹

ANNUAL INCOME	MARGINAL TAX RATE
up to \$14,000	10.5 cents
from \$14,001 to \$48,000	17.5 cents
from \$48,001 to \$70,000	30 cents
\$70,001 and over	33 cents

PAYE (as a payroll tax) is paid as the employee earns income. PAYE is deducted at source and remitted at the appropriate rate (annualised for employees) and paid to the Inland Revenue Department ("IRD"), New Zealand's taxation authority. Accordingly, it is an employer's responsibility to correctly calculate an employee's PAYE, deduct that from earnings to which the employee is entitled and to remit that sum to the IRD when an employer is required to do so. An employee will not have any involvement in calculating and paying this PAYE component; that responsibility falls to their employer in managing payroll. From an employee's perspective, there is no involvement in the mechanism by which this PAYE tax is actually paid.

An employee will also be required to make contributions towards New Zealand's Accident Compensation Scheme by way of ACC earner levies. The rates of those levies are set annually by law and are currently:²²

	EARNER'S LEVY RATE	MAXIMUM INCOME EARNER'S LEVY CHARGED ON	MAXIMUM LEVY ANYONE CAN PAY
Employee	\$1.70 per \$100 (1.70%)	\$116,089	\$1,973.51
Self-Employed	\$1.70 per \$100 (1.70%)	\$113,768	\$1,934.05

All employees subject to PAYE have an additional ACC contribution deducted from their PAYE. As such, in the same way as PAYE, employees have no involvement in this calculation and remission to the IRD.

¹⁹ See, for example, *Cardy Business Limited v Bizaoui* (2005) 2 NZELR 245 (EC), *Tse v Ciefte (NZ) Limited* [2009] ERNZ 20 (EC), *Downey v New Zealand Greyhound Racing Association Inc* (2006) 3 NZELR 501 (EC) and *Chief of Defence Force v Ross-Taylor* [2010] NZ EmpC 22.

²⁰ Above n19.

²¹ <http://www.ird.govt.nz/how-to/taxrates-codes/itaxsalaryandwage-incometaxrates.html>.

²² <http://www.ird.govt.nz/income-tax-individual/different-income-taxed/salaries-wages/acc>.

Independent contractors are not subject to the PAYE system. Depending upon the nature of the services that an independent contractor provides they may be subject to payment of withholding tax. Withholding tax implies a contract for services, as it is a form of provisional tax obtained at a lower rate than most PAYE deductions and it entitles the reimbursement of business expenses through tax returns.²³ Different rates are applicable to different types of services. The party engaging such an independent contractor is required to deduct withholding tax and remit that to the IRD, however, an independent contractor remains liable for his or her own ACC earner levies and ultimately for payment of income tax above the amounts remitted through.

If a person establishes a company in order to provide their services as an independent contractor then that person will be required to pay company tax on all profits earned by the company in its financial year.

The current rate of company tax is 28 cents on the dollar for all profits earned in the 2016 income year.²⁴ If the contractor does not trade through a company or other relevant vehicle, he or she will be liable to pay income tax at the same personal rates as an employee, set out above.

If an individual or entity is registered for the Goods and Services Tax (the current threshold above which registration is mandatory is \$60,000 of turnover per annum)²⁵ then that individual is required to levy an additional 15% as GST for a taxable supply of goods and services. The levy is required on any good or service produced and sold or supplied by the person. The individual or entity is able to claim an imputation of 15% for GST expended. The net sum of GST levied and expended is then required to be remitted to the IRD on either a quarterly or six month basis in settlement of a person's GST obligations. In many cases, an independent contractor will be required to register for GST because their taxable supply of services will exceed \$60,000 per annum.

c. Differences in Benefit Entitlement

Employees are entitled to various benefits by law as a result of their status as employees. In particular, the Holidays Act 2003 (the "HA") provides a suite of benefits for the purposes of certain types of leave. Those forms of leave are annual holidays, public holidays, sick leave and bereavement leave.

The purpose of annual leave is to allow an employee an absence from their employment for the purposes of rest and recreation.²⁶ An employee who has completed 12 months' continuous employment with an employer is entitled to four weeks' annual leave in that year and in each subsequent 12 month periods of employment.²⁷ An employee is entitled to take a period of annual leave and to receive payment at the greater of their average weekly earnings or ordinary weekly earnings at the time at which the annual leave is taken.²⁸ That payment is made to the employee in the period to which the annual leave relates.²⁹ An employee who ends their employment within the first 12 months is entitled to payment of the accrued amount of annual leave at 8% of their gross earnings since they became employed.³⁰ An employee who completes 12 months' continuous employment, but does not take their full entitlement to annual leave is entitled to similar payment on termination of employment.³¹

²³ Schedule 4 Income Tax Act 2007

²⁴ <http://www.ird.govt.nz/how-to/taxrates-codes/bit-taxrates-companytax.html>.

²⁵ Section 51 Goods and Services Tax Act 1985.

²⁶ Section 3(a) HA 2003.

²⁷ Section 16 HA 2003.

²⁸ Section 21 HA 2003.

²⁹ Section 27(1) HA 2003

³⁰ Section 23(2) HA 2003

³¹ Sections 24 and 25 HA 2003.

All employees are entitled to public holidays under the HA. The purpose of public holidays is to observe certain days of national, religious or cultural significance.³² The HA prescribes 11 days which are public holidays in New Zealand for which employees are entitled to observe these days as leave from their employment.³³

A person may be entitled to payment for public holidays. If the day would “otherwise be a working day” for the person (i.e. the person would be working on the day but for the public holiday occurring) then they are entitled to be absent on the day and to receive their relevant daily pay for the day.³⁴ If the day would not otherwise be a working day for the employee then they are not entitled to payment for the public holiday if they do not actually work on the day.³⁵ If a person works on the public holiday they are entitled to time and a half of their relevant daily pay for all hours worked on the day.³⁶ If the day would otherwise be a working day for the employee then, in addition to time and a half of their relevant daily pay for working on the day, an employee is entitled to an alternative day’s holiday to be taken at a later date in substitution for the public holiday.³⁷

The HA provides for sick leave for employees for the purposes of recovering from sickness or illness, or to care for a person who depends on the employee and who is sick or injured.³⁸ A person is entitled to five days’ sick leave after six months’ continuous employment, and to a further entitlement for each subsequent 12 month period of employment.³⁹ Fifteen days’ sick leave can be carried over from one period of entitlement to another up to a total of 20 days’ sick leave in any one period.⁴⁰

An employee is entitled to bereavement leave for the purposes of recognising the death of a relative or for the death of a person where it is accepted that the person has suffered a bereavement.⁴¹ For certain categories of familial relationships, a person is entitled to three days’ bereavement leave.⁴² In any other case where the employer accepts that the person has suffered a bereavement, the employee is entitled to one day’s bereavement leave.⁴³

An independent contractor is not entitled to any form of leave under the HA, because the Act applies strictly to employees.⁴⁴ Accordingly, in situations where an independent contractor may wish to take leave for any of the reasons provided for by the HA it will ordinarily be taken by the person as unpaid absence.

The KiwiSaver Act 2006 (the “KS Act”) is applicable for the majority of New Zealand employees.⁴⁵ KiwiSaver is a work-based contribution scheme to private superannuation accounts for individuals. Membership is voluntary for employees. If a person is a KiwiSaver member and an employee, then the person will be required to make employee contributions to their scheme.⁴⁶ The employee contribution rates that an employee must elect are 3%, 4% and either 8% of gross salary or wages.⁴⁷ An employer is required to calculate the employee’s contributions and deduct that at source from an employee’s

32 Section 3(b) HA 2003.

33 Section 44 HA 2003.

34 Section 49 HA 2003.

35 Section 48(1) HA 2003.

36 Section 48(1) HA 2003.

37 Section 50 HA 2003.

38 Section 56 HA 2003.

39 Section 3(c) HA 2003.

40 Section 65(2) HA 2003.

41 Section 66(2) HA 2003.

42 Section 3(d) HA 2003.

43 Section 69(2)(a) HA 2003.

44 Section 69(2)(b) HA 2003.

45 Section 7 HA 2003.

46 Section 6 KS Act 2006.

47 Section 66 KS Act 2006.

pay during payroll.⁴⁸ The employer is then required to remit the KiwiSaver deductions to the IRD for onward transmission to the employee’s KiwiSaver provider.

At the same time, an employer is required to make compulsory employer contributions to an employee’s KiwiSaver scheme.⁴⁹ The current contribution rate is an additional 3% of an employee’s gross salary or wages.⁵⁰ That additional amount is required to be transmitted to IRD for onward transmission to the employee’s KiwiSaver provider.⁵¹

An independent contractor is not entitled to receipt of employer contributions to KiwiSaver as the employer contribution rules only apply to employees. However, any New Zealand citizen or person entitled to be in New Zealand indefinitely is entitled to become a member of KiwiSaver.⁵² Accordingly, if the person is not employed, but is an independent contractor they can still make their own contributions to KiwiSaver.⁵³ An independent contractor can therefore maintain their own KiwiSaver scheme, but will not be entitled to any form of employer contribution.

There are various other forms of benefits that apply to employees in the form of tax credits and parental leave payments, which may or may not apply to independent contractors.

d. Differences in Protection from Termination

New Zealand’s employment framework is protectionist in the sense that employees are protected from unjustified dismissal. In essence, this protects an employee from dismissal except for cause. The limited exception to this is that an employer is entitled to terminate a person’s employment within the first 90 days of employment if an employee is employed on a “trial period” allowing for termination within this initial period.⁵⁴

The Act provides that, outside a trial period, an employee may only be dismissed if the employer’s actions in doing so and how the employer acted were within the scope of what a fair and reasonable employer could have done in all the circumstances at the time the dismissal or action occurred.

The Act provides for a system of “personal grievances”. An employee has a personal grievance if, during the course of their employment, their employer takes any action against the employee which disadvantages them or dismisses them and which is not justified with reference to the section 103A test.⁵⁵ Personal grievances may be raised by an employee, for determination by the Employment Relations Authority. The personal grievance system allows for reimbursement of monies lost as a result of the grievance⁵⁶ and to compensation for hurt and humiliation suffered as a result of the unjustified actions by the employer.⁵⁷

As they are not subject to the provisions of the Act, independent contractors are not entitled to personal grievance remedies, nor are they entitled to the protection that section 103A of the Act affords. In contrast, these individuals are only entitled to the protections that the common law provides, or are provided by the Contractual Remedies Act 1979 in terms of contractual remedies.

48 Section 64 KS Act 2006.

49 Section 67 KS Act 2006.

50 Subpart 3A KS Act 2006.

51 Section 101D(4)(c) KS Act 2006. 191 SecZon 93 KS Act 2006.

52 Section 6 KS Act 2006.

53 Sections 95 and 96 KS Act 2006.

54 Sections 67A and 67B of the Act

55 195 Section 102 and 103 of the Act.

56 Section 123(1)(b) of the Act.

57 Section 123(1)(c)(i) of the Act.

If an independent contractor has a claim for breach of contract for which damages are sought, he or she would be required to issue any such claim in the Courts of ordinary jurisdiction. The independent contractor's remedies would ordinarily be the contractual remedies provided by the common law and the Contractual Remedies Act 1979. While the authority also has the power to provide for ordinary contractual remedies arising out of an employment relationship, it has access to the additional remedies provided by the personal grievance system.⁵⁸

Further, the authority is empowered to order reinstatement of an employee to their former position or to a position no less advantageous to the employee in the event that they have been unjustifiably dismissed.⁵⁹ Reinstatement must be a remedy claimed by an employee in order for it to be awarded by the authority.⁶⁰ In determining whether reinstatement should be ordered, the authority must consider whether reinstatement is both "practicable" and "reasonable".⁶¹ That remedy is not available to independent contractors.

e. Local Limitations on Use of Independent Contractors

There are very few limitations on the use of independent contractors in New Zealand law.

There are some limited restrictions on the characterisation of workers as employees. The Act precludes volunteers who receive no reward for work as a volunteer from being characterised as employees. The Act also excludes from the definition of an employee a person who is engaged in "film production work" in any capacity, unless the person is specifically employed on a written employment agreement providing that the person is an employee.

The film production work exception was a recent amendment to the Act, which arose in late 2010 as a result of the production of The Hobbit movies in New Zealand. The amendment related to a dispute between the producers of the films and certain New Zealand unions involved in representing various performers and others engaged in providing services to the films. The provision was intended to clarify the supposed contractual uncertainty in the film industry as a result of the Bryson decision. Individuals in the film production industry are therefore normally engaged as independent contractors rather than employees.

f. Leased or Seconded Employees

There is nothing in New Zealand law that prevents or regulates employees from being leased or seconded. Likewise, there is nothing that otherwise generally regulates the terms of "triangular" relationships. Those relationships are therefore subject to the section 6 test. However, where a person has structured their arrangement to introduce a corporate vehicle into their arrangement (or some other additional party) it is more likely that they will not be considered to be an employee for the purposes of the Act.⁶²

g. Regulations of the Different Categories of Contracts

Should an independent contractor have issues with his or her contract and is not seeking to be declared an employee pursuant to section 6(5) of the Act, the contractor may seek to have the contract enforced by filing civil proceedings in the District or High Courts on New Zealand.

⁵⁸ Section 162(c) of the Act.

⁵⁹ Section 123(1)(a) of the Act.

⁶⁰ Section 125(1) of the Act.

⁶¹ Section 125(2) of the Act, see also *Angus v Ports of Auckland Limited* [2011] NZEmpC 160.

⁶² *McDonald v Ontrack Infrastructure Limited* [2010] NZEmpC 132.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

Re-characterisation of the Relationship

It is open to a person to apply to the authority for a declaration that they are an employee. The authority then applies the test provided in section 6 in deciding whether or not to provide the declaration sought. Section 6(5) of the Act provides:

It is open to a person to apply to the authority for a declaration that they are an employee. The authority then applies the test provided in section 6 in deciding whether or not to provide the declaration sought. Section 6(5) of the Act provides:

- (5) *The Court may, on the application of a union, a Labour Inspector, or 1 or more other persons, by order declare whether the person or persons named in the application are—*
- (a) *employees under this Act; or*
 - (b) *employees or workers within the meaning of any of the Acts specified in section 223(1).*
- (6) *The Court must not make an order under subsection (5) in relation to a person unless—*
- (a) *the person—*
 - (i) *is the applicant; or*
 - (ii) *has consented in writing to another person applying for the order; and*
 - (b) *the other person who is alleged to be the employer of the person is a party to the application or has an opportunity to be heard on the application.*

In practice, however, re-characterisation is most commonly attempted by a person after a relationship, which on its face is an independent contracting relationship, has been terminated. In that case, the person will attempt to raise a personal grievance⁶³, and the alleged employer will defend that personal grievance on the basis that the person is not an employee. In the ordinary course of events, the authority will resolve the person's personal grievance by first resolving a preliminary question regarding whether the person is, in fact, an employee, following which the authority will determine whether their personal grievance(s) can be pursued.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

As outlined above, while section 6(3) of the Act provides that the authority may not treat as a determining matter any statement that describes the nature of a relationship, parties to an independent contracting relationship should properly record its terms in writing.

In order for a principal to ensure, as far as possible, that a person engaged as an independent contractor is not an employee, the contract should provide that the person is in all respects an independent contractor and not an employee, partner or subsidiary of the principal. The contract should make clear that the independent contractor is solely

⁶³ See below "Differences in ProtecZon from Termination".

liable for all of its debts, losses, expenses and taxation on its income. The contract should also provide that the person will not at any stage, either during or subsequent to the termination of the contract, allege that the person is an employee of the principal.

It would also be expected that the rates paid for services will be expressed with reference to GST, and that payment for services would be following provision of an invoice. Additional matters, which will separate an independent contracting arrangement from an employment agreement will include provisions addressing indemnification, warranties and insurances. Parties to such an agreement should also consider whether the dispute resolution provisions of the Arbitration Act 1996 can be incorporated into their agreement. Each of these matters is not commonly provided for in ordinary employment agreements and, accordingly, may assist in establishing, consistent with the relevant tests that the intention of the parties was to enter into a contracting relationship.

Finally, it would be expected that a person be encouraged to obtain legal advice at the time that the independent contractor agreement is negotiated.

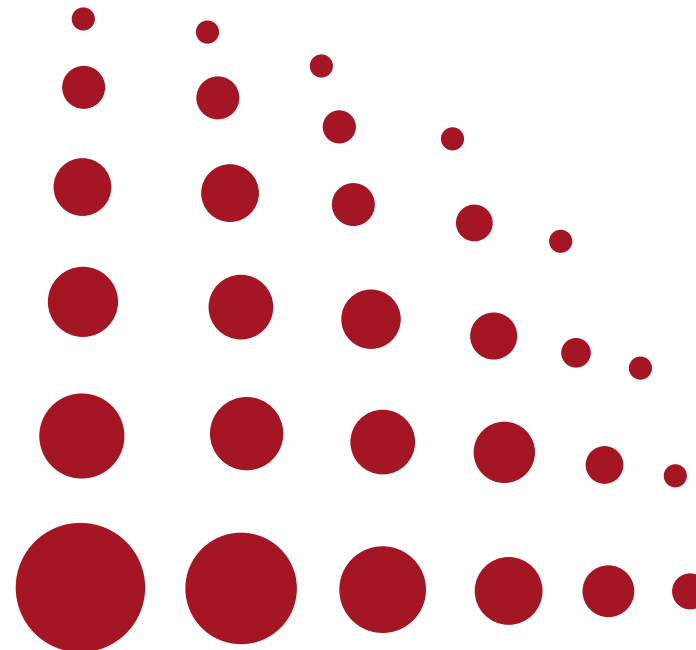
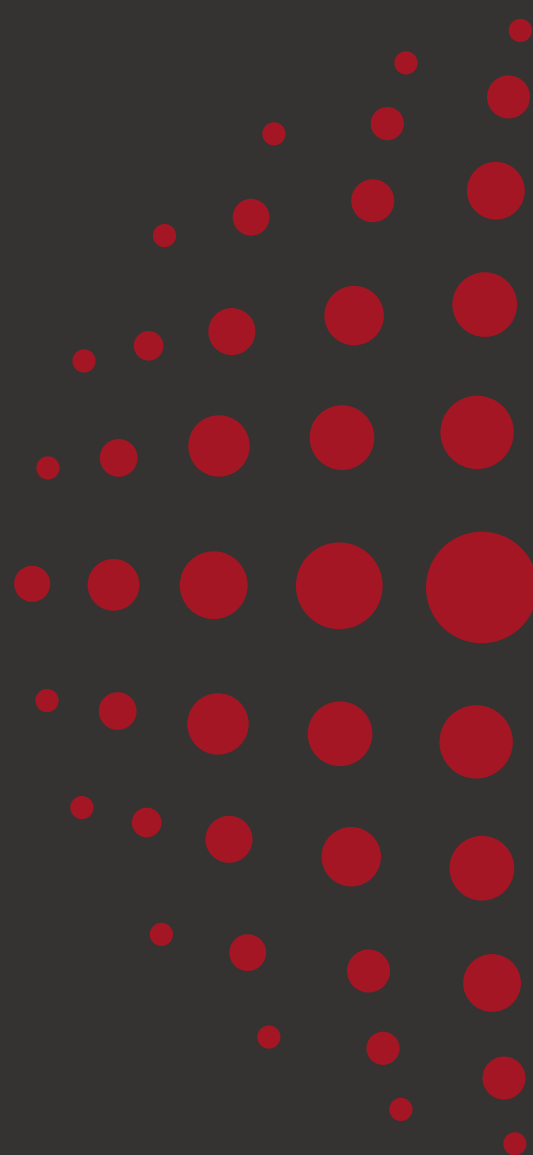
b. Day-to-Day Management of the Relationship

At all stages of the relationship with an independent contractor, consideration should be had to whether, applying the common law tests, there may be a risk that the person is in fact an employee. If that is the case, then there should be consideration of whether it is appropriate to terminate the independent contractor agreement and re-engage the person as an employee. Doing so potentially reduces the risk of re-characterisation at a later time. It may be that the individual confirms his or her desire to be engaged as an independent contractor notwithstanding the risk of a later re-characterisation. In those circumstances, those discussions/negotiations should be documented as a way to demonstrate the clear intent of the parties.

V. CONCLUSION

Section 6 of the Act requires the authority to consider the real nature of the relationship between parties in order to determine whether a person is an employee or independent contractor. In making its determination, the authority will apply the common law tests of control, integration and the fundamental test, together with a consideration of the terms of the written agreement. Plainly, cases under section 6 are heavily fact specific. Therefore, while statements of principle such as those outlined above assist determination of status, the intensely factual nature of cases make trends in this area difficult to determine.

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NORWAY

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I. OVERVIEW

The Working Environment Act only applies to employees and not individual contractors and the distinction between the two terms are therefore important. The term “employee” is briefly determined in the Working Environment Act. However, the distinction between the terms “employee” and “individual contractor” is at large developed through case law.

a. Introduction

The Working Environment Act applies to any undertaking that engages employees, and it covers most aspects of employment, including working time, health, safety, environment, and job security. Opposite, the Working Environment Act does not apply to situations where the undertaking is not engaging an employee, but rather uses independent contractors. Consequently, the distinction between employees and independent contractors is an important one. Should the undertaking be wrong in assessing the distinction, the undertaking is responsible for the consequences.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The difference between an employee and an independent contractor in Norway is based on whether or not the person performing a work task is determined to be an “employee” according to the 2005 Norwegian Working Environment Act (“Arbeidsmiljøloven”). Similar definitions are relevant for tax treatment and benefit entitlements.

The notion of “employee” is a discretionary term. The meaning of this term is determined by case law. Based on this case law, the distinction between an “Employee” and an “Independent Contractor” is made by the questions of:

- Which party is responsible for the result of the work that is performed?
 - *The most important rule is that the independent contractor bears the risk of delivering a specific result, whether this is to deliver a finished project or build a house. The "employee" however, is responsible for performing his work tasks as best as he can from day-to-day, leaving the responsibilities for the result to his employer.*
- Is the person performing the work tasks obligated to follow the other party's day-to-day instructions, or can he decide for himself how to receive the result he is supposed to deliver?
 - *If the person performing the work tasks is obligated to follow the other party's day-to-day instructions, he is most likely seen as an "employee".*
- Is the person performing the work obligated to perform the work personally, or can he use another person to perform the duties to fulfill his obligation?
 - *If the person performing the work tasks is obligated to perform the work personally, this is seen as a sign that he is an "Employee". If he can use another person to deliver his result, he is more likely an independent contractor.*
- Which party is responsible for the work tools and assets that are necessary to perform the work?
 - *If the person performing the work tasks holds his own work tools, he is more likely*

an independent contractor than if he uses the other party's tools and assets. In many cases, however, this can be different due to the character of the services delivered.

- Is the person performing the work tasks only working for one principal, or does he have several customers?
- *If the person performing the work tasks entitled to have many customers and actually able to do it, he is more likely an independent contractor than a person who is obligated to only work for one customer.*

b. General Differences in Tax Treatment

The Employer must pay the Social Contribution Tax, calculated on the salary, which the employee is paid. Furthermore, the employee shall pay income tax.

The independent contractor, however, is obligated to pay taxes and VAT himself.

c. Differences in Benefit Entitlement

An employee is entitled to holiday pay from the employer, while the independent contractor is not. In addition, an employee is entitled to official sick pay and earns official pension benefits through the Social Benefits Act. Employers are also obligated to establish a private collective pension scheme for all employees.

The contractor has to pay or cover these kinds of benefits himself.

d. Differences in Protection from Termination

Independent contractors are not protected from termination at all – their rights related to termination are solely based on the wording of the contract. Employees in Norway are, however, protected from unfair dismissal by the 2005 Working Environment Act. The validity of these contracts and termination of such contracts are regulated by the 1918 Contracts Act and general Civil law.

According to the 2005 Working Environment Act section 15-7, an employee may not be dismissed unless this is objectively justified on the basis of circumstances relating to the enterprise (redundancies).

One typical example of circumstances connected with the enterprise is rationalisation measures. Dismissal due to these circumstances is, however, not objectively justified if the employer has other suitable work to offer the employee in the enterprise. Further, when deciding if a dismissal on these grounds is warranted, the needs of the enterprise shall be weighed against the inconveniences a dismissal will involve for the individual employee.

Each employee must be evaluated individually. This implies that there can be just cause for notice in relation to one employee, but not in relation to another employee.

Further to the Norwegian court practice the relevant selection criteria include:

- competence (e.g. education and work experience, quality of performance);
- seniority;
- personal suitability (e.g. leadership abilities, cooperation);
- social aspects (e.g. family responsibilities/financial situation, health, age, opportunities in the job market).

For a dismissal to be “fair” grounded on non-performance from the employee, an employer must be able:

- to prove that the employee was very well aware of what kind of performance was required from him, including his work tasks and other kinds of obligations;
- to prove that the employee did not perform in accordance with the employer's requirements;
- to prove that the employee was informed regarding his discrepancies and was given a chance or to improve his performance but did not do so.

Based on these guidelines, every case has to be considered individually.

e. Local Limitations on Use of Independent Contractors

There are no limitations.

f. Other Ramifications of Classification

The Working Environment Act regulates maximum working hours for employees on a daily, weekly or yearly basis. The Norwegian Labour Inspection Authority enforces the provisions, and if they are found to be breached, the undertaking may be fined. However, these provisions do not apply for independent contractors.

In accordance with the Working Environment Act chapter 10, working hours is the time, during which the employee is at the disposal of the employer, while off-duty time is the time, during which the employee is not at the employer's disposal. Pursuant to section 10-2 (1), working hours shall be arranged in such a way that employees are not exposed to adverse physical or mental strain, and that they shall be able to observe safety considerations.

Normal working hours must not exceed 9 hours per 24 hours and 40 hours per 7 days, cf. section 10-4 (1) and pursuant to section 10-11 (1) such hours shall normally be scheduled between 6 a.m. and 9 p.m. Work lasting more than 5 ½ hours a day shall be interrupted by at least one break. The break shall be at least one hour if the working hours are at least 8 hours per day.

Furthermore, working hours must be arranged so that the employee has at least 11 hours continuous off-duty time per 24 hours (daily off-duty time), which shall be placed between two main work periods. Furthermore, the employee is entitled to a continuous off-duty period of at least 35 hours per 7 days (weekly off-duty time). Night work and work on Sundays may only be imposed as far as prescribed by law, cf. sections 10-10 and 10-11.

Work in excess of what the Working Environment Act prescribes as normal working hours, are regarded as overtime work, cf. section 10-6 (2). Overtime work must not take place except in cases when there is a specific and time-limited need for it, and must not exceed 10 hours per 7 days, 25 hours per 4 consecutive weeks or 200 hours during a period of 52 weeks. For overtime, work a supplement of at least 40 per cent shall be paid, in addition to the pay received by the employee for corresponding work during normal working hours, cf. section 10-6 (11).

g. Leased or Seconded Employees

The other typical mechanism in Norway is the use of temporary work agencies, with the main purpose of hiring out their employees to other companies hiring an extra workforce without having to employ them. The “hiring out” is defined as situations where:

"the employees of the provider of labour are placed at the disposal of the principle (the requisitioner of labour) and are subject to the principle's management and instructions. The requisitioner also has the financial risk for the result of the work. The employees hired on are employed by the provider. The provider is responsible for payment of salary, etc. and is responsible for ensuring that the employees hired on possess the qualifications assumed for the assignment."

The Supreme Court ruled in June 2013 regarding the difference between a subcontractor company and a company hiring out their employees:

The case was filed by an employee employed by a subcontractor / temporary agency, who had handled one of the oil company Statoil's internal post offices for many years. This employee had been working at this internal post office as an employee of the subcontractor / temporary agency and not by Statoil. As Norwegian law provides that an employee hired out from a temporary agency for more than 4 years is entitled to employment from the requisitioner of labor, he filed a court case claiming that the contractual relationship between Statoil and his employer was a hiring contract and not a subcontracting agreement. Consequently, he claimed permanent employment with Statoil.

Due to the same points as stated under section I a) above, the contract was ruled as a subcontract and not a hiring from a temporary agency. The most important point was that the employees employer was responsible for delivering a finished result to Statoil, a post office, and not only responsible for delivering a group of employees.

This group of hired out employees are covered by the Temporary Agency Work Directive, and are entitled to primarily the same salary and working conditions as if they were employed directly with the company hiring them in.

It is important to note that hiring of labour from temporary-work agencies is only lawful in cases where temporary employment is permitted. Hiring of labour may therefore be an alternative to temporary employment in connection with unforeseen peaks and seasonal fluctuations.

h. Regulations of the Different Categories of Contracts

In Norway, the different groups of contracts are defined by mandatory legislation in regards to employment law, tax law and social benefits law. If an individual is not considered an "Employee", the relation is regulated by the general civil law. Consequently, there are very few case related to these issues.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

A re-characterization may take place if the person performing the work tasks is judged as an "employee" according to the 2005 Working Environment Act, the 1988 Holiday Act or the 1997 Social Benefits Act.

A kind of re-characterization may also take place if the tax authorities conclude that the payment for work tasks performed by a person in reality is a payment for a work performance done as part of an employment relationship.

b. The Legal Consequences of a Re-Characterisation

If the person who has performed work tasks for the employer is re-characterized as an "employee" by the courts, the re-characterized employee is normally entitled to permanent employment with the employer. This gives him full protection from the 2005 Working Environment Act, related to i.e. protection against dismissals, working time and overtime regulations. In addition, an employee is entitled to holiday pay in accordance with the 1988 Holiday Act and full social benefits according to the 1997 Social Benefits Act. In addition, see section d) below.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The person Seeking "Employee" status may seek negotiations, but will normally have to file a lawsuit in the Courts claiming his employee status.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

If the employee is granted "employee" status according to the 2005 Working Environment Act, he may be entitled to compensation for any economic loss or holiday pay for the last 3 years.

If the re-characterization is done by the tax authorities related to tax questions, both the employer and the person performing the work tasks may be liable for extra tax payments and punitive tax payments. Such tax obligations may be claimed for work performed during the last 10 years.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

If you want to properly document that a relationship is with an independent contractor and not an employee in reality, you need to make sure that the contract between the party is clear on the facts that:

- you must describe a precise "result" that the contractor is responsible for delivering, and not only for performing day-to-day tasks within his field of expertise.
- normally, the "result" will indicate a kind of temporary period until the result is actually delivered. Estimated delivering dates may be practical. In other cases this will not be practical, cf the "Foster Mother" case as described under section V below.
- the payment is based on delivering of results and not on hours spent working.
- it is the contractor's responsibility to use his own tools, unless the work performed is dependent on tools and assets from the principal company.

In addition, it is important that you, during the work period, document that the provisions as mentioned above are also respected during the contract period.

Especially from a tax perspective, the independent contractor should be registered with his own company, and preferably as a company and not a sole proprietor.

b. Day-to-Day Management of the Relationship

It is important that the day-to-day management of the relationship with an independent contractor is based on the respect that the contractor is not one of your employees

and is not supposed to be instructed as if he was an employee. The more the principal company feels the need to instruct and control the contractor's day-to-day work, the more it is possible that he will be considered as an employee by a court.

It is also important that the invoice from the independent contractor is based on the delivery of a defined target and not based on the number of hours work has been performed.

The normal situation is that independent contractors are performing work for you for a temporary period of time, even if this time period may not be that specific. In some businesses we find very long relationships, where the independent contractor has performed his work tasks for the same company for 10-15 years. These kinds of more permanent work by independent contractors may more easily be seen as a "hidden" employment relationship.

If the contractor is able to actually perform work for other principals in addition to you, this would indicate that he actually is a contractor and not an employee.

V. TRENDS AND SPECIFIC CASES

Trends

As the labour market in Norway is very good from a European perspective with regards to the employees or independent contractor's possibility to find work, many people performing the work want to be independent contractors. When the market is good, many persons prefer the freedom of being independent, in addition to the payments that are most often higher than for employees.

During times where the market is not so good, however, or the person performing work tasks becomes ill or in need of other kinds of benefits, we have the court cases related to the distinction between employees and independent contractors.

Many employers also tend to use independent contractors instead of own employees, especially when it comes to jobs within the IT sector or the building / construction sector. When considered independent, the employers free themselves from benefits and especially the strong protection against dismissals of employees. Due to the implementation of the Temporary Agency Work Directive and the very strict conditions for hiring from temporary agencies, we see a trend where the use of independent contractors are even more interesting for employers than before.

Recent Case Law

In 2013, the Norwegian Supreme Court announced two verdicts regarding the difference between an "employee" and an "independent contractor". The first judgment was related to a municipal "support contact" for a family, while the other case was related to a foster mother.

In the two cases the "support contact" had made a claim for holiday pay. The foster mother, however, had made a claim for sick pay. In both cases, they had contracts with a municipality as "independent contractors". In the first judgment, the "support contact" was considered to be an "employee" with the right to holiday pay. In the second judgment, the foster mother was considered to be a real "independent contractor".

The Supreme Court mentions 7 points to take into consideration when defining whether or not a person is an "employee". The Court also states that these points must be reviewed on a discretionary basis from case to case:

- the duty to perform the work personally and not use substitutes
- the duty to subordinate and follow the employers instructions and control
- the employer holds the work premises, equipment etc.
- the employer is responsible for the result of the work performed
- the payment is executed by some kind of salary
- the contractual relationship is stable, with an agreed period of notice
- the work is mainly performed for 1 single principal
- when there is doubt, the answer must come from a discretionary review where all points are taken into consideration.

In addition to these 7 points, the Supreme Court based their decision on whether practical circumstances should indicate that the person was an employee or an independent contractor. In the last judgment regarding the foster mother, the majority of the judges regarded foster care as such a distinctly different relationship as a normal employment relationship, as the core tasks of foster care is to take a foster child into their home to, as much as possible, become part of the foster mother's own family.

In 2016, the Supreme Court assessed the notion of "employee" once again. The question was whether a person acting as a reliever for a family with a boy with Downs syndrome and also acted as the child's support person pursuant to the Health and Care Services Act, was considered an employee in the municipality in which she resided. The Supreme Court used the 7 points to distinguish between employee and independent contractor. The Supreme Court found that the point on duty to subordinate and follow the employer's instruction and control was pivotal in the assessment. Even though actual instructions were not given, it was sufficient to state subordination for the person at hand. Other factors that could indicate that she was an independent contractor were found not to change the overall assessment, which concluded that she was an employee.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

The term "permanent establishment" is defined in the Nordic tax treaty. Permanent establishment means a fixed place of business through which the business of an enterprise is wholly or partly carried on. The term permanent establishment includes especially:

- a place of management a branch
- an office
- a factory
- a workshop, and
- a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

A building site or a construction, installation or assembly project, or activities consisting of planning, supervising, consulting or other auxiliary work by personnel connected with such a project, constitutes a permanent establishment only if the project lasts more than 12 months and is carried out in the same place. When a person is acting in another Nordic country on behalf of an enterprise and he has, and habitually exercises, an authority to conclude contracts in the name of the enterprise, the enterprise shall be deemed to have a permanent establishment, so-called dependent agent. An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

In Norway, “*permanent establishment*” as a kind of “*permanent work place*” is defined as “*the place where you normally perform your work tasks*”.

VII. CONCLUSION

The use of independent contractors – as well as subcontracting companies – is increasing in Norway. The reasons for this may be numerous, but we believe an important reason is the Norwegian employers’ belief that the protection against dismissals in Norway is especially high (if an Employer actually follows the law, however, it is not especially difficult to terminate an employment relationship in Norway).

The distinction between an employee and an independent contractor in Norway is defined by mandatory law interpreted by the courts, both regarding employment protection, holiday pay, tax, pension and social benefits. These definitions are very similar, but the cases related to tax law indicates a somewhat different evaluation as the topic is not protection of individuals, but the question of tax liability for companies and individuals.

When having to distinguish between an employee and an independent contractor, the content of the contract is very important. The most important factor is, however, the question of how the parties conduct themselves during the day-to-day management.

The main indicator when deciding whether or not a contractual relationship is considered as employment or not, is the question of whether or not the contractor is responsible for the results of his work or only for using his expertise and doing his best for a period of hours or days.

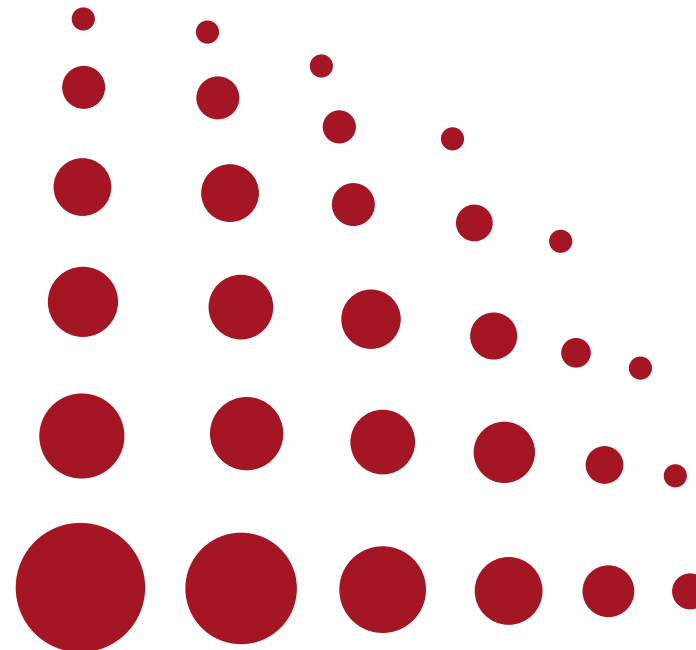
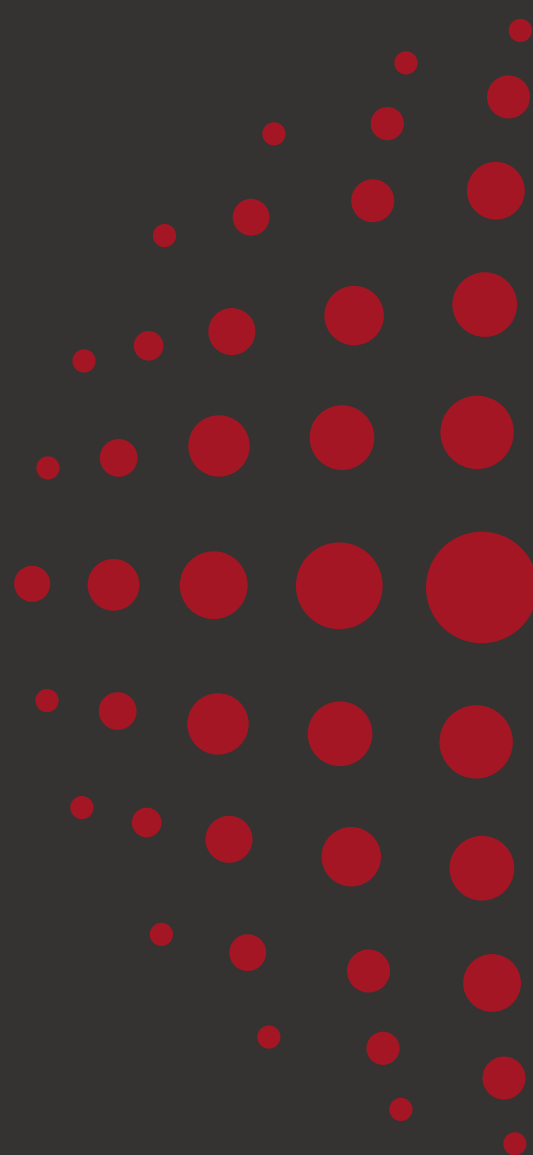
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POLAND

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I. OVERVIEW

Choosing Independent Contractors instead of relationships based on contract of employment is increasingly popular in the Polish labour market. As the labour market becomes more complex and it continuously develops, the trend is clearly visible for both parties – entities, which require human labour and persons offering their services. As per Polish Central Statistical Office's information dated 27th of January 2016 Independent Contractors constitute 6,9% of all employed persons in Poland. For most of Independent Contractors (92,5%), this form of employment constitutes the only work they perform. This phenomenon is caused either by the contractor's will or the principal's will. As per research made by Central Statistical Office, 80,2% of persons who worked based on civil law contracts, worked in this form not due to their choice. Furthermore, more than the half of Independent Contractors were hired in this form, as it was the only acceptable form of relationship for employers.

Four fifths of Independent contractors are persons who concluded a contract of mandate or service contract to which provisions regulating a contract of mandate are applicable. Acting as an Independent Contractor is most commonly seen among persons under 24 years old and above 60 years old. These numbers clearly show that non-employment contract based forms of employment shall be much more significant part of labour market in the years to come.

a. Introduction

The Working Environment Act applies to any undertaking that engages employees, and it covers most aspects of employment, including working time, health, safety, environment, and job security. Opposite, the Working Environment Act does not apply to situations where the undertaking is not engaging an employee, but rather uses independent contractors. Consequently, the distinction between employees and independent contractors is an important one. Should the undertaking be wrong in assessing the distinction, the undertaking is responsible for the consequences.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

In Poland, the legal basis for performing work may be based on a relationship governed by civil law or by administrative law, or the employment relationship. The most common form of performing work is either performing it within the employment relationship based on contracts regulated by the Labour Code, or within the framework of civil law contracts ('contract of mandate', contract for a 'specific task') regulated by the Civil Code.

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Performing work on the basis of the contract of employment

Definitely the most common contract regulating the performance of work is the contract of employment. Polish law provides for several types of such contracts. The Labour Code lists the following contracts: for a trial period, for a fixed period and for an indefinite period. Only an individual person having the capacity to conclude the contract of employment may be an employee. The employer, on the other hand, may be a legal person as well as a natural person, and also an organizational unit without the status of a legal person, if they employ workers. Therefore, one does not have to run a business to be an employer.

The Polish Labour Code lists the obligatory elements of every employment relationship. This listing can serve as a basis for the construction of a legal, positive definition of the employment relationship concept. The employment relationship arises when an

employee undertakes to perform work of a specified type for the employer, under the employer's supervision and in the place and time indicated by the employer, and the employer commits itself to employing the worker for remuneration. It is, therefore, a mutually binding relationship, in which the two parties to the contract, both the employee and the employer, are at the same time bound and entitled to specific considerations. However, the fact that the contract of employment is mutually binding does not at all result in the considerations of the parties being always mutual and fully equivalent.

According to the rulings of the Supreme Court, the constitutive elements of each employment relationship, which always have to occur jointly, are: voluntary character of performing the work, personal performance of the work in a continuous manner, the employee's subordination to the employer, performing work for the employer, and the paid character of employment.

The voluntary character of performing work by an employee assumes in the first place that forced labour is inadmissible. The Constitution of the Republic of Poland specifies that the obligation to work may be imposed only by law (art. 65 par. 2 of the Constitution of the RP). At the same time, the voluntary character of performing work manifests itself in the fact that an employee is not obliged to perform work of another type other than that resulting from the content of the concluded contract of employment. Thus, the employer cannot order an employee to do work of a type different than the type specified in the contract, unless there is a clear statutory base. Otherwise, this could be considered as forced labour. An employee's consent to perform a different type of work alone is not sufficient, either. If the parties intend to permanently change the type of work performed by the employee, they have to change the terms of the contract either by terminating these terms, or by mutual agreement.

The employer may demand personal performance of work from an employee. Therefore, it is not admissible for an employee to relieve himself from his obligation to perform work by appointing a replacement or a subcontractor. Even in the case of a passing obstacle in personal performance of work (e.g. the employee's illness), the employee cannot authorize a third person to perform the work in his place.

The employment relationship is a continuous relationship, which should be understood functionally, as being performed in a repeated manner. The employment relationship cannot be reduced to a one-time action or a one-time completion of a certain work. The continuity of the employment relationship does not mean that it has to be performed every day. It is important for the work to be performed in a repeated manner, so it is acceptable that work is performed either on an everyday basis or in specified intervals of time.

Another, crucial and characteristic element of the employment relationship is the employee's subordination. It is the employer who manages the work of his employees, and it is he who decides about the way it is to be performed. An employee cannot decide about the way the work is to be performed, even if he were a specialist in a given field, and even if it could result in a positive outcome for the employer. The employer may give the employee binding orders relating to work which, unless illegal, have to be respected by the employee. In the body of the Supreme Court's rulings, failure to carry out the employer's orders at work without a legally justified reason is considered to be a gross violation of the employee's basic duties, and such behaviour by an employee justifies the termination of the employee's contract of employment without notice (so called disciplinary dismissal).

Performing work for the employer means that, as a rule, the effects of an employee's work and the profits thereof should belong to the employer. This does not mean that the effects of the employee's work can be used or consumed only by the employer. The

employer has the effects of the work of his employees at his disposal. The effects of an employee's work, as long as their properties allow it, can be the subject of a sale contract between the employer and a third party (e.g. a work produced by the employee, a work made as part of the employment), and they can even be abandoned, destroyed, or disposed of. As a rule, however, a situation where the effects of an employee's work go exclusively, or in the first place, to a third party that is not the employee's employer is inadmissible. An exception is temporary employment, under which an employee who is employed by a temporary employment agency performs work for and under the supervision of a third entity which is not his direct employer (the so called user employer). The construction of temporary employment resembles the lease institution in property law, and being an exception from the principle of work for the employer, it is regulated in whole outside the Labour Code in the Temporary Employment Law.

Work based on an employment relationship can be performed only for remuneration. An employee's obligation to perform work "for free" is invalid. Furthermore, an employee cannot effectively relinquish his right to remuneration. However, it is admissible to perform work at no charge outside the employment relationship, e.g. as a voluntary service, gratuitous training, or under a civil contract.

Work performed within an employment relationship is characterized by the fact that it is performed "at the risk" of the employer. In an employment relationship, the employer's risk appears in three forms. The first is personal risk – it is the employer who bears the consequences for non-culpable mistakes made by an employee in the process of work. In other words, an employee is not responsible if, despite his efforts and good intentions, he fails to achieve the effects of his work expected by the employer, or even those he himself expected. The employer's second type of risk is the economic risk – the employer is responsible for the economic results of the business he runs. Thus, even if the financial balance is negative, the total loss of the workplace bears on the employer and not the employees, even if the loss is caused by failure to reach the assumed effects by the employees. The employer's third type of risk is the technical risk – the employer is obliged to meet his obligation to an employee even during disturbances in the functioning of the workplace. A situation where an employee does not work because, for example, the workplace does not have orders for a specific product, the production line has broken down etc. does not free the employer from the obligation to pay the remuneration for the time of such stoppage.

The above means that a contract of employment is a best-efforts contract rather than a contract to achieve a specific result. The parties to a contract of employment cannot specify in a binding way the expected results of the work and to make the employee's right to receive remuneration dependent on these results. It results from the nature of the employment relationship that an employee is to perform employee actions in a manner adequate to the type of work and possessed skills, and as effectively as possible.

Work based on a civil law contract

The actual actions defined as "work" by one entity for another entity are not always performed and do not always need to be performed on the basis of a contract of employment. The rising trend to use civil law contracts in place of the contracts provided for in the Labour Code is caused mainly by the obligations which the employer has to meet when concluding a civil law contract and, to be more specific, the obligations which the employer does not have to meet in a civil relationship. The Labour Code is employee-centred, which means that the labour law regulations, and definitely the legal scholars and case-law, are centred on the so called protective function of labour law. According to the currently prevalent trend, labour law should protect the employee, as the weaker party of the employment relationship, from the stronger party. As can be observed in practice, contracts of employment are less common in the market and more often replaced by civil law contracts at a rate directly proportional to the process of increasing

employee protection. From the employer's point of view, these latter contracts ensure better flexibility of labour (among other things, regulations regarding working time do not apply to such contracts), offer a greater ability to react to changes in the workplace, as they arise by allowing easier termination of the legal relationship between the parties, and above all, they lead to reduced labour costs, which seems to be the strongest argument in today's economic relations.

The Polish Civil Code provides for several contracts by which one of the parties commits itself to performing certain actions for the other party. These contracts are 'contract of mandate', 'contract for a specific task' and 'contract of agency'.

The contract of mandate is the most frequently occurring civil-law basis of providing services (including work). As specified in legal regulations, by entering into a contract of mandate, the party receiving the mandate (the 'mandatary', or simply the contractor) commits itself to performing a specified legal action for the person granting the mandate (the 'mandator' or simply the employer) - art. 734 of the Civil Code. Although a strict interpretation of the quoted regulation does not seem to include the performance of factual mandatory actions (e.g. work), the opinion that factual actions can also be performed on the basis of the contract of mandate is justified by the reference that the regulations regarding the contract of mandate should be applied to all contracts for providing services not regulated in the Civil Code.

Both natural persons and legal persons may be parties to a contract of mandate. The contract of mandate cannot be concluded by an organizational unit, which does not have the status of legal person, because a party needs to have full capacity to legal transactions to conclude the said contract. Also a minor, who does not have at least a partial capacity to legal transactions, as well as a fully incapacitated person, cannot enter into a contract of mandate.

The Civil Code introduces the presumption that a contract of mandate is entered into for remuneration. Thus, if the parties agree that the party receiving the mandate will perform a certain legal or factual action for no remuneration, then the mandate will be free of charge. If there is no clear indication by the parties that remuneration will not be due for the accomplishment of the mandate, the person receiving the mandate is entitled to a remuneration corresponding to the performed work, unless the parties specified the amount of the remuneration in the contract.

The mandate relationship lacks subordination, which is characteristic of labour law, and the contractor does not remain at the disposal of the employer. However, the employer may give the contractor instructions regarding the way of performing the mandate. Even then, the contractor may withdraw from carrying out such instructions if a situation occurs where obtaining approval from the mandator is not possible and there are reasons to believe that the mandator would approve the change if he or she knew the actual state of affairs. Therefore, the contractor has much more freedom during the performance of the work based on the contract of mandate because, as indicated above, an employee performing work on the basis of the contract of employment may never withdraw from the way of performing the work as indicated by the employer, unless such way violates the law.

As a rule, the contractor should perform the mandate in person. However, this is not an unconditional regulation, as withdrawal from personal performance is allowed either on the basis of the concluded contract, if the parties provided for such possibility, or if such possibility is allowed by custom, or if the contractor is forced to do so by the circumstances. In the latter case, the contractor will be responsible for damages, if such damages are caused by entrusting the performance of the work to a third person (subcontractor).

The contract of mandate, like a contract of employment, is a best-efforts contract. The mandatary is not required to achieve specific results. He is only to perform the agreed actions in a manner adequate to the type of work and possessed skills, and as effectively as possible. The fact that the contract of mandate is a best-efforts contract distinguishes it from another civil law contract, the contract for a specific task.

As the Labour Code regulations do not apply to contracts of mandate, persons carrying out a mandate have only such rights as result directly from the content of the concluded contract.

The contract of mandate provides the parties with an option to freely specify the place and time of performing the work. The place where work is to be performed can be either a workplace or any other place specified by premises or by area, not excluding the contractor's home. Also the working time is freely specified by the parties, because the parties are not restricted by working time limits, or daily or weekly periods of uninterrupted rest.

By entering into the contract for a specific task the person taking the order undertakes to perform a specific task, and the person placing the order, to pay remuneration (art. 627 of Civil Code). It follows from the above that the contract for a specific task is, like the contract of employment and the contract of mandate, a bilaterally binding agreement. It is also a contract for remuneration. The feature which very clearly distinguishes the contract for a specific task from the contract of employment and the contract of mandate is its character – because it is a contract for a result. The parties to the contract define within it a specific, individual result, which can have both a corporeal (e.g. preparing an opinion, a list) or incorporeal (e.g. giving a lecture) character.

The contract for a specific task does not assume personal performance by the person taking the order. If, however, the performance of the work depends on specific, individualized attributes of the contractor (e.g. preparation of a legal opinion by an indicated individual lawyer), then the obligation to perform personally must be assumed. Such situations should be settled by the content of the contract.

As regards the contractor's rights, the definition of the place of work, the working time etc., the comments referring to the contract of mandate remain applicable to the contract for a specific task as well. That is so, because the parties to the contract for a specific task may freely agree on all issues not prohibited by law, in agreement with the principle of the autonomy of the parties.

b. General Differences in Tax Treatment

Conclusion of a contract under which an employee will perform work, both a contract of employment and a civil law contract, gives rise to obligations of a public nature. These obligations are: payment of the personal income tax advance to the tax office and payment of contributions to the Social Insurance Institution (ZUS). The amount and type of deductions from the employee's remuneration depends on the type of the concluded contract.

Contract of employment – social insurance contributions and funds, income tax advance

When concluding a contract of employment, the parties are obliged to bear the public burdens. The first such burden is the personal income tax advance paid to the tax office. The way of calculating the amount of the tax is regulated by the income tax law. The amount of the tax is calculated by the employer and the employer is obliged to pay the said tax to the tax office. The amount of the tax advance depends on the amount of pay due to the employee. Although the tax is paid by the employer, it is charged to

the employee, because the amount is deducted from the remuneration received by the employee.

Another public burden connected with the contract of employment is social insurance contributions. In the employment relationships, the parties are obliged to pay contributions to ZUS in respect of the following insurances: retirement pension, disability pension, sick benefits, and health insurance, as well as the contributions for the Labour Fund and the Guaranteed Employee Benefits Fund.

The insurance contributions are paid by both parties, in different amounts. The employee finances a part of the contributions for the retirement pension, disability pension, sick benefit, and health insurances. The rest of the above contributions are financed by the employer. The employer is also responsible for financing the contributions for accident insurance and employee funds.

Civil law contracts

A person entering into the contract of mandate is liable for the following compulsory insurances: retirement pension insurance, disability pension insurance, and health insurance. In addition, a person performing work on the basis of the contract of mandate in the seat of the employer is liable for compulsory accident insurance. The sickness insurance is voluntary.

The compulsory social insurances (retirement and disability) and the health insurance are also compulsory for contractors who have already acquired the right to the retirement or disability pension.

On the other hand, the compulsory social insurance and the health insurance do not apply to students up to 26 years old performing a contract of mandate.

Contrary to the contract of mandate, the contract for a specific task is not an independent title to insurance. The social insurance and health insurance contributions have to be paid only if the parties to the contract for a specific task are also parties to an employment relationship. Therefore, if the only relation between the parties is the contract to perform a specific work, the employee does not need to be covered by any insurance.

The employer is obliged to pay income tax on each civil law contract. Depending on the amount of the remuneration received by the person performing work under a civil law contract, the employer pays either the income tax advance or a flat rate tax. These questions are regulated by income tax law.

c. Differences in Benefit Entitlement

All employee benefits are regulated by labour law. These regulations are not only the regulations of the Labour Code, but also of other laws. Additional entitlements may also be granted to employees by internal sources of labour law, such as work and pay regulations, the collective agreement, and also by individual contracts of employment.

As a rule, only employees performing work on the basis of the contract of employment have the right to the above mentioned employee entitlements. The regulations under discussion apply to such employees *ex lege*.

Persons performing work under a civil law contract have no rights to any employee entitlements based on labour law. This is connected with the fact that they are covered neither by Labour Code regulations nor by other sources of labour law. The above means that regulations concerning such issues as the minimum wage, working time standards, the admissible number of overtime hours and work on Sundays and public holidays,

annual leave, or maternity leave do not apply to employees performing work on the basis of the contract of mandate or the contract for a specific task.

This does not mean that the parties to a civil law relationship cannot decide about the application of these regulations to independent contractors. Such practice is fully admissible. Freedom of contract allows the parties to commit themselves to apply the regulations in a specific way, including both the generally binding (the Labour Code, common acts) regulations and the in-house sources of labour law. Such commitment of the parties does not, however, result in that the employer or the employee will be responsible for infringements of labour law according to the rules provided in the Labour Code. Owing to the fact that the parties' obligation to apply labour law is only a civil obligation, if they infringe the regulations, they will be liable for damages under the Civil Code for failure to perform or inadequate performance of an obligation (art. 471 KC).

Due to the practical purpose of concluding civil contracts, which is making the employment relationship more flexible and exempting the employer from applying Labour Code regulations, situations where the parties to a civil contract voluntarily agree to apply labour law regulations will definitely be marginal.

d. Differences in Protection from Termination

As indicated above, the regulations of the Labour Code apply exclusively to the parties to the employment relationship. They do not apply to civil obligations. This also refers to the conditions of terminating contracts of employment.

Termination by notice and termination without notice of a contract of employment

The Labour Code introduces a number of regulations restricting termination by notice and termination without notice of contracts of employment. In most cases, these restrictions concern the employer. An employee, as a rule, does not have to justify a termination of the contract of employment at all. The only case where the employee should specify a justification of his decision of termination is when the cause of the termination is mobbing and the employee demands compensation.

The Polish Labour Code distinguishes the common and special protection against termination of the contract of employment by employer.

The common protection covers only contracts of employment concluded for an indefinite period. For the employer to be able to legally dismiss a person employed on the basis of such contract there must be a specific, justified reason for dismissal. In addition, the reason must be firstly an objective reason, because subjective feelings of the employer towards an employee do not justify a dismissal, and secondly, the reason for dismissal must actually exist and the burden of proof of its existence rests upon the employer. The Labour Code does not contain a catalogue of events, which would justify an employee's dismissal by notice. As the Code uses a blanket clause, directions should be looked for in case-law. And so, according to the rulings of the Supreme Court, in a specific situation, the reason justifying termination by an employer of a contract of employment concluded for an indefinite period can be *inter alia*: inability to work in a team, repeated and long-lasting absences caused by sickness, lack of the employee's cooperation with the employer, professional uselessness or incapability, minor violation of employee duties which do not justify a disciplinary dismissal, alcohol consumption at work or appearance at work in a state of intoxication, behaviour against the principles of community life, the employee's irascibility, or theft of the employer's property. Clearly, the catalogue of reasons is not a closed catalogue. Whether a given reason is justified or not can be decided only in a specific individualized actual situation.

The **special protection** against termination of the contract of employment applies to employees who, due to special circumstances, are entitled to a temporary limitation of the possibility to terminate their contract. And so, according to the Labour Code, the employer cannot terminate the contract of employment with an employee who lacks not more than 4 years to his or her retirement age, if the employee's seniority allows him to acquire the right to retirement pension by reaching this age. Also, the employer cannot terminate by notice or without notice an employment contract with a pregnant woman or during her maternity leave, unless there are reasons for disciplinary dismissal. The employer is not free to terminate the contract with a person who is a member of or has a specific function in a trade union, both at the company or above-company level. Labour law regulations require either consultation with the relevant labour union before terminating the contract of employment in the former case, or the union's consent to the termination in the latter.

The requirements for the existence of a justified reason for the termination of the employment contract, and for a statement of that reason in the text of the notice by employer, applies only to contracts for an indefinite period. Therefore, legal termination of contracts of employment for a fixed period does not depend on the existence of any reason. Nonetheless, on the grounds of the Polish Labour Code, not every fixed-period contract can be effectively terminated.

The notice period for the contract for a trial period depends on the period for which the contract has been signed and it ranges from three working days to two weeks. The replacement contract may be terminated with a notice of three days. Apart from the above, generally employment contracts (fixed term and for an indefinite term) may be terminated with a notice period dependent on the period for which the contract has been signed and it ranges from two weeks to three months.

Termination of a civil contract

Due to the already discussed fact that the regulations of the Labour Code do not apply to civil law contracts (mandate and specific task), their termination is regulated in the Civil Code. From the point of view of the person performing the work, these regulations are unquestionably less favourable, as they neither offer protection against unjustified dismissal in such extent as labour law regulations do, nor do they provide notice periods. Therefore, a contract of mandate or a contract for a specific task can be terminated overnight if the contract does not provide for otherwise.

According to the regulations of the Civil Code, the employer may withdraw from the contract at any time before the completion of the work, but then he is obliged to pay the agreed remuneration after deducting the amount, which the contractor saved due to the non-completion of the work.

A similar situation applies to the contract of mandate, - the employer ('mandator') may withdraw from it at any time, but he should return the expenses incurred by the contractor ('mandatary') to properly perform the obligation. In addition, if the mandate was paid, the mandator is obliged to pay a part of the remuneration corresponding to the mandatary's actions so far. If the termination was without an important reason, the mandatary is obliged to return any incurred damage. The restitution for damage in the case of termination without important cause resembles the construction of employer's liability for unjustified termination of the contract of employment. However, in the case of termination of the contract of mandate, the employer's liability will be civil liability. The amount of compensation will not therefore be limited as is the case with contracts of employment, but the contractor will not have a claim for the completion of the mandate or the work in imitation of the claim for reinstatement in employment provided in labour law.

Of course, in the civil contract, in compliance with the principle of freedom of contract, the parties may both include the reasons for termination and introduce the notice period. These will not be, however, labour regulations, but civil regulations, and hence the claims can be sought for only under the Civil code.

e. Local Limitations on Use of Independent Contractors

Polish law does not restrict the use of civil contracts. The parties are completely free to choose the basis for employment. Furthermore, there are no general rules concerning specific types of work or positions on which employees may be employed exclusively on the basis of the contract of employment or exclusively on the basis of a civil contract.

It should be remembered that the substitution of a contract of employment by a civil law contract while maintaining the terms of employment as specified in the Labour Code is inadmissible. Therefore, if an employee undertakes to perform work of a specific type (1) for the benefit of an employer, (2) under the employer's supervision, (3) and in a place and time fixed by the employer, (4) the work will be performed on the basis of the contract of employment, even though the parties label it a contract of mandate or a contract for a specific task. The establishment of the employment relationship is automatic if all the conditions defined by the Code are fulfilled. This is understandable, as contracts of employment are socially more readily acceptable than civil law contracts, which is the reason why the legislator introduced the described mechanism.

Additionally, the Penal Code contains penal regulations according to which an employer employing an employee on the basis of a civil law contract in a situation in which according to the Labour Code the employer should conclude a contract of employment with the employee commits an offence and thereby is liable to a fine of PLN 1,000 to 30,000 (EUR 250 to 7,500).

f. Leased or Seconded Employees

In today's social relations, a certain level of flexibility in the employment relationship is desirable. This is understandable, since it is mainly the employer who bears the burden of comprehensive care for the prosperity of the workplace, and who carries the economic risk carried by running a business and employing people therein. If an employer is to quickly react to the demand of the market and the workplace, he must have at his disposal a mechanism of "shifting" free labour forces to places where, in the given moment, the demand for labour is the greatest.

A constitutive element of every contract of employment includes the parties defining in the employment relationship, the type of work performed, the place of work, the amount of the remuneration, and the working time (full- or part-time). As mentioned above, the requirement to specify the type of work to be performed by the employee in the contract is the consequence of the constitutional prohibition of forced labour. An employee has to agree to the type of work performed, and the employer cannot unilaterally order an employee to perform work other than what was agreed upon. Besides protection against forced labour, the definition of the type of work in the contract of labour is an element organizing the employment relationship, and the definition of the type of work offers the employer the ability to indicate duties which are connected with the given position and which the employee is obliged to carry out.

To reconcile the employees' right to confidence in the type of work performed with the employer's right to flexibly use the employees' potential, not to allow a situation where employees are forced to perform labour which has not been agreed on (forced labour), and at the same time influence employment flexibility, the Polish legislator included into the Labour Code the construction of secondment (temporary transfer) of an employee

to other work/other place of performing work.

Secondment (temporary transfer) of an employee to other work/other place of performing work

Change of the type of work performed by an employee is, as a rule, possible by a notice altering the terms of work. However, regulations about termination of contracts apply to a termination of the contract terms and therefore, in the case of contracts concluded for an indefinite period, the employer may terminate the terms of such contract only when there are justifiable reasons to do so. A corresponding application of the regulations about the final termination of contracts of employment to the altering termination, leads to a conclusion that the termination by the employer of the terms of contracts (and therefore of the type of work performed) with a pregnant employee, an employee during maternity leave, and an employee during the pre-retirement protection period, as well as an employee who is a member of a union or who has a specified union function, is not admissible without consultation with that union.

The Polish Labour Code provides for one exception to the above rule. The employer has the right to unilaterally transfer an employee to other work if all conditions provided in the Code have been fulfilled. The employer has the right to temporarily transfer an employee to other work without the need to terminate the terms of work of such employee in the following situations: the existence of a reasonable need of the employer (1) and in addition, the other work has to correspond with the employee's qualifications, (2) the period of secondment cannot exceed three months in a given calendar year, (3) and the secondment to other work cannot cause a reduction in remuneration (4).

When all of the above conditions have been fulfilled, secondment of an employee to another type of work is allowed. The secondment we are talking about can refer not only to the type of work, but the place in which it is performed, as well. For the employer, the advantage of a secondment under the said Labour Code regulation is that the employer does not have to bear additional costs, e.g. travelling expenses, which in lack of secondment would be associated with the necessary business trip to another place of work.

Temporary employees

A form of employment relationship, which makes this relationship more flexible is the institution of temporary work. The Temporary Employees Employment Law of July 9, 2003, implementing Council Directive 91/383/EEC of June 25, 1991, introduced the notion of temporary employment to the Polish legal order. Since then, this peculiar form of employment has become a stable element of the Polish labour market. The reasons for the popularity of temporary employment are complex. It seems that the party who benefits the most from this form of employment is the employer, though certain advantages for temporary employees can be seen, as well. This applies particularly to novice employees on the labour market and employees who have other duties in addition to work. It seems plausible to theorize that the greater the inflexibility of typical employment (based on the Labour Code), the more popular temporary work will become. Temporary employment is characterized by the fact that the user employer for whom and under whose supervision the temporary employee performs work, does not remain in a legal relationship with the latter.

A temporary employee is employed by a temporary work agency for a fixed period of time or for the time of performing a specific work. Between the agency and the temporary employee there is a classic employment relationship regulated by the Labour Code. The user employer is not an employer within the meaning of the Labour Code for the temporary employees. On the basis of an agreement with the agency, the temporary employee is sent to work at the user employer's workplace, the user employer being a third person for the temporary employee.

Due to the fact that an employment relationship occurs between the temporary work agency and the temporary employee, duties resulting from this relationship rest with the agency and the employee, and not with the user employer. That is why the user employer does not pay remuneration to the temporary employee. The user employer's duties towards the temporary employee are limited exclusively to those provided for by law (e.g. assurance of safe and healthy working conditions, assurance of the use of the annual leave by the temporary employee) or those agreed upon with the temporary work agency, which has "rented out" its employee.

The above means also that the user employer cannot terminate the employee's contract of employment. This can be done only by the temporary work agency. If the user employer desires to end the employment of a temporary employee, it will be necessary to terminate the legal relationship between the employer and the agency.

An employer who intends to "rent" an employee from a temporary agency agrees with this agency in writing on the type of work to be entrusted to the temporary employee, the qualifications required to perform the work with which the temporary employee is to be entrusted, the expected period of performing the temporary work, the working time of the temporary employee, and the place of performing the temporary work. Additionally, the user employer informs the temporary work agency in writing about the remuneration for work which is to be entrusted to a temporary employee, specified in wage regulations in force at the user employer's workplace, and about the conditions of performing temporary work regarding health and safety at work.

The user employer's duties towards a temporary employee are generally limited to obeying industrial safety regulations, keeping of the employee's working time records, granting the annual leave due to the employee, and non-discrimination in employment. These duties may be extended in the contract with the temporary work agency. Such provisions, however, will be civil obligations and not labour obligations and, in addition, the person entitled to claim damages in court will not be the temporary employee, but the temporary work agency.

From the relation linking the temporary work agency with the user employer, arises the agency's liability for damage done to the user employer by the temporary employee. The agency's liability is based on the Civil Code.

A temporary work agency bears liability for damages in case the user employer infringes on the rule of equal treatment in employment with regard to the temporary employee. This is understandable, because there is no employment relationship, which could be a basis for liability, between the temporary employee and the user employer. The temporary agency is entitled to a recourse claim towards the employer "renting" an employee in respect of paid compensation.

g. Regulations of the Different Categories of Contracts

Contract of mandate

The purpose of the contract of mandate is to provide the mandator with specialized services of the Contractor. The Contractor is to perform a set of specified actions on behalf of the mandator. What is worth to be noticed is the fact that the contract of mandate generally expires in case of the death of the Contractor. In case of death of the mandator it is presumed to be still in force. It is the manifestation of the rule of protecting the justified interests of the mandator and his heirs. Contract of mandate is recognized as a contract of thorough action. It means that results of contract should be judged not by the final result of actions of the Contractor but by the way he performed his obligations. It means that the Contractor is responsible not for the final outcome of his actions but for the utmost good faith in exercising his duties towards the mandator.

Currently, contract of mandate is encompassed with obligatory payment of contribution to the Social Security Fund, unless the Contractor meets the requirements of release from the mentioned obligation. They vary and are based on such conditions as: the age of the Contractor, being in employment relationship with the Principal or being registered as a student.

Contract for a specific task

The contract of performing a specific task is a civil-law-based contract concluded between the ordering party and the accepting party. The accepting party commits to create a specific task and the ordering party commits to pay remuneration. A specific task can be any material thing or immaterial composition (e.g. computer program).

Obligation of the accepting party consists of executing such a chain of activities that in the end result in creation of a specified task. As for the obligation of the ordering party, promised remuneration should be clearly stated in the contract, not necessarily in the form of amount of money that is to be paid. Instead, parties can agree to calculate final amount of remuneration based on some factor of a certain value and a numerical factor.

The specific task can also be of a non-material character, especially when it has to do with the creative activity- e.g. with creating a poem or a song.

Contract of performing a specific task is a contract of a result. It means that judging whether it was performed properly should be based on the characteristic of the final outcome of the contract- the specific task- and not on the actions that were undertaken in order to create mentioned task.

Even though the contracts on performing a specific task are not encompassed with obligatory payment of contribution to the Social Security Fund, they are often controlled by the appropriate authorities in order to check if they do not hide actions that otherwise should be viewed as performed under the contract of mandate. It is done to ensure that individuals do not avoid paying mandatory payments to the Social Security Fund.

Agency agreement

This is a contract in which the agent commits to be a constant intermediary in terms of concluding contracts between the Principal and his clients or to conclude mentioned contracts in the name of the Principal. Obligation of the principal consists of paying the remuneration to the agent. Both agent and the principal are to be entrepreneurs and the agent is additionally obliged to act within the scope of activity of his company.

This contract can be concluded in any form. Written form is prescribed by the Civil Code only in a situation in which the agent commits to bear liability for performing duties of the clients' arising from the contracts concluded between them and the Principal.

Management contract

Management contract is a contract, which is neither named nor defined by Civil Code. It is not identical to any other contract. As a result it is defined as an "innominate contract". The essence of this contract is to act in the name and on behalf of company. As it is a contract of due diligence a manager is not obliged to achieve a specific result but manager has to assure the highest degree of professional care and conduct. Manager is neither a subordinate nor under management of mandatory.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Replacement of the contract of employment by any civil law contract while maintaining the terms and conditions of labour employment is not admissible under the regulations of the Polish Labour Code. Conclusion of a contract by which one of the parties undertakes to perform work of a specified type for the other party, under its direction and in the indicated place and time, and the other party commits itself to pay remuneration for work causes ex lege the emergence of the employment relationship between the contracting parties, irrespective of the name of the contract concluded by the parties. The main intention of this regulation is to prevent the pathology consisting in labour law evasion in relations between employers and employees.

b. The Legal Consequences of a Re-Characterisation

The consequence of the conclusion of a civil law contract while keeping the terms and conditions of labour-code employment, is that the employee may submit claims for ascertainment of the existence of an employment relationship. An employee with whom a civil law contract has been concluded on the terms of the contract of employment may submit the case to the labour court and demand the ascertainment of the relationship. Such a claim may also be filed by a non-governmental organization within its statutory activities, if the employee agrees. Also, a labour inspector may institute an action against the employer if a civil law contract is found to have been concluded on the terms of a contract of employment. In the judicial proceedings, both the NGO and the labour inspector are a party in the formal (for the purpose of court proceedings) sense, as there is no legal relationship between them and the sued employer.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Despite the code prohibition on conclusion of civil law contracts on the terms of the contract of employment, this regulation is very often bent nowadays. That is because civil law contracts are more favourable to employers, as they are free from most obligations, which would be a burden to them under the regulations of the Labour Code. The action for the ascertainment of the existence of the employment relationship is meant as a remedy for this practice and protection of employees' interests.

A demand for the ascertainment of the existence of the employment relationship can be made if there is suspicion that a given person was not employed on the basis of a civil law contract, but a contract of employment. The action may be brought to the labour court by any person who has a legal interest in the case.

The petitioner can be either an employee who claims to have been a party to an employment relationship, or a Labour Inspector. In the latter case, there are two options. The Inspector can demand the ascertainment of the existence of the employment relationship on his own initiative, which does not require approval of the person for whom the Inspector acts, but he may also join any pending proceedings, to which however, the person who has brought the case to court has to consent. Other persons may also demand the ascertainment of the existence of the employment relationship, even though this relation does not concern them directly, if they can prove their legal interest. For example, such persons can be relatives of a deceased employee who, in their opinion, was employed on the basis of a contract of employment.

When deciding whether a given relationship had the character of an employment relationship, the labour court takes into consideration the will of the parties to the concluded contract and the features of the relationship between the parties. In most

cases, the features typical for civil law contracts and contracts of employment overlap, so the court has to establish which of those features prevail. It is not possible to unambiguously outline the practice in a case of ascertainment of the existence of the employment relationship, as everything depends on the specific facts of the case. The court indicates the prevalence of specific features of the contract and can either allow the claim and pronounce the existence of the employment relationship, or dismiss the claim.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The possibility that the court may ascertain the existence of the employment relationship is not the only consequence of concluding a civil law contract on the terms of the contract of employment. The Labour Code contains penal regulations according to which an employer employing an employee on the basis of a civil law contract in conditions where, in compliance with the Labour Code, this employer should conclude the contract of employment with this employee, commits an offence and is subject to a fine of PLN 1,000 (ca EUR 250) to PLN 30,000 (ca EUR 7,500).

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Performance of work on the basis of a civil law contract is not governed by labour law regulations, which has already been mentioned many times. That is why regulations describing the way of documenting the employment relationship do not apply to civil law contracts.

In the first place, it is not necessary to open and keep the employee's personal file in a civil relationship. Such files are a peculiar set of documents appearing only in the employment relationship, and collecting data regarding an employee outside this relationship is inadmissible in view of the Personal Data Protection Law.

In a civil relationship, it is also not necessary to record the employee's working time, since neither daily nor weekly working time limits apply to such an employee. An employee employed on the basis of the contract of mandate or a contract for a specific task enjoys a relatively large flexibility of performing work, at least from the theoretical point of view. Of course, there is nothing to prevent the parties from specifically indicating in the contract what working time limits will apply to the employee. The employer also has the full right to document the working time of employees performing work on the basis of civil law contracts, if only for accounting purposes. However, this will only apply to the employer's internal documentation and only for the employer's use.

During the whole period of the civil relationship on the basis of which the employee performs work, and until claims that could arise from this relationship fall under the statute of limitation, the employer should keep the original document or a certified copy of the concluded contract for evidence purposes. Although evidence from hearing witnesses or the parties is admissible in proceedings before a civil court, a document, as long as its credibility is not questioned, has a definitely stronger legal validity than testimony. Besides, especially if the parties fixed numerous detailed provisions of the contract, differing from regulations that are standard in the given relationship, proving such provisions before the court can be extremely difficult without a written contract.

b. Day-to-Day Management of the Relationship

As a general rule, elements specific for the employment cannot be included in other contractual relationship to the extent making mentioned relationship basically equivalent to the one of employment, only named differently. That being said, contracts basing on performing certain tasks in a specific place cannot be supervised to the full extent. This does not mean however that some level of supervision, expressly stated in provisions of law cannot be enforced. This point of view is applicable for both contract of mandate and contract for a specific task.

Contract for a specific task consists in creation of a specified good by a contractor. It is obvious that mentioned good has great (personal if not economical) value for a person initiating relationship for creation of a specific task. Often, deadline set by parties for a completion of a good has value equal to the value of the good itself, e.g. when specified good is to be used only once for a very special occasion. It is vital for a person initiating performing a specific task to have a control over the process of performing itself. Otherwise, this party would not be able to substitute this specific good with another one, created by other performer. This clearly shows how important is the institution of supervision in a contract for a specific task. However, having in mind what was said about the prohibition of creating a contract of employment under a different name, it is vital to state what rules of managing the concluded relationship, are created by provisions of law.

Firstly, polish civil code provides the party ordering the specific task with possibility to renounce the contract in case of the contractor being in such a delay with completion of the contract that it is highly implausible for him to fulfil his part of obligation on time. Secondly, the ordering party can demand change of way in which the task is performed if it is improper to a large extent. What is more, cooperation between parties is essential also for the proper completion of task and under certain circumstances can become a justified reason for dissolution of a contract. Powers mentioned above cannot be executed without constant and actual management of the relationship binding the parties- such conclusion is devoured from reasoning implying that duties arising from provisions of law must be accompanied by powers that make them possible to be fulfilled (the reasoning from the goal to the measures).

When it comes to the contract of mandate, provisions of law expressly provide the Principal with possibility to be informed about the process of executing the contract. As a general rule, such informational duty burdens the Contractor only to such an extent that is justified by the nature of a contract. Completion of one part of obligation and beginning of subsequent steps should be notified to the Principal. It is done in order to provide him with information necessary to assess if the Contractor is fit to fulfil obligations entrusted to him and further existence of the contract retains its economically justified character to the Principal.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The growing importance of civil law contracts as well as increasingly more common use, at least at the statistical level, of temporary employment, signifies a tendency among employers to "free" themselves from the employment relationship in favour of more employer-friendly relationships. Rules governing the labour market are relentless and in every situation the general mechanism of performing work will tilt towards economically more favourable solutions. The legislator, for the time being, is turning the scale towards solutions that are more favourable socially, which understandably mean solutions less

economically favourable for the labour market. Although the social character of labour law is economically favourable for employees, it is certainly not the case for employers. And, since employers employ employees and not the other way round, they are not willing to accept more public duties towards the employees. As a consequence of that, employees employed on the basis of contracts of employment, are squeezed out of the labour market, by persons performing work on the basis of civil law contracts. This closes the vicious circle into which the legislator seems to fall sometimes, when by introducing into the Labour Code regulations intended to protect employees, the legislator leads de facto to a situation where employees are losing jobs. The less flexible the model of an employment relationship, the less frequently it will be used by potential employers.

b. Recent Amendments to the Law

Act on minimal remuneration

Starting from 1st January 2017, there will enter into force the amendment to the Act on minimal remuneration (Journal of Laws of 2002, no. 200 item 1679). Its provision now will create a rule that not only those hired on a full time job, but also those performing their duties based on civil-law contracts to an extent comparable to labor-law based employment have to be awarded on the basis of the same single hourly rate amounting for 12 zlotys gross per hour. Minimal hourly remuneration is to be adapted in accordance with growth rate of minimal remuneration that was based on employment contract.

Such a regulation was created in order to curb the practice of abusing usage of civil-law contracts to perform duties that otherwise would be performed by employees hired on an employment contracts, the former being obviously underpaid for executing the same duties.

From now on, contractors will have to be awarded minimal wage. What is more, it has to be paid in cash. Employers will not be able to substitute part of wage with products manufactured by the contracting company. Payment of the remuneration has to be done at least once a month; contractors will not be able to be granted full remuneration effective on the completion of the contract. The legislator finally took a position that secures the interests of contractors. Role of their remuneration is to provide them with financial resources necessary to survive. In situation when the term of the contract was excessively long, there was a huge risk that they will stay without resources needed to lead a decent life.

Remuneration is to be calculated on the basis of hours actually worked. The way in which they will be established was left for the parties to decide. The Contractor will provide the employer with calculation of worked hours and the latter will either accept it or express comments.

Additionally, bonus for work during work time, differently than up to now, will not be calculated into the minimal remuneration. This provision favors those receiving minimal remuneration for their work, as until now, mentioned bonus was included into minimal wage, effectively even decreasing their hourly rate.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

Conclusion of a civil law contract by a company having its seat outside the territory of Poland, with a Polish national, for performing work in the territory of Poland, does not give rise to tax or insurance obligations of that employer towards the appropriate Polish

offices. Such contracts, as a rule, are governed by the national law of the employer. Tax obligations (income tax), if any, may concern the employee performing work in Poland for a foreign entity.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

Employment of a Polish national on the basis of the employment contract in the territory of Poland, by an employer who has neither its seat nor a branch in Poland can, contrary to civil law contracts, give rise to certain obligations.

If the employer is an undertaking from an EU country, such employer must register itself as a payer of the Polish insurance contributions with ZUS and pay social insurance contributions for the employed employee. This duty arose with Polish accession to the European Union, i.e. on 1 May 2004. Due to the fact that the abovementioned duties could discourage an employer from the EU (the language barrier, international transfers), it is possible to shift them to the employee employed by the foreign undertaking. This requires an agreement between the EU employer and the employee who is to perform work in Poland. Under such agreement, the duties of the payer (filing of the forms and payment of the contributions) will be shifted to the employee.

If the employer is an undertaking from outside the European Union and it has neither a seat nor a branch in Poland, the duty to pay social insurance contributions does not arise. The employee will be free to decide whether he will pay such contributions or not.

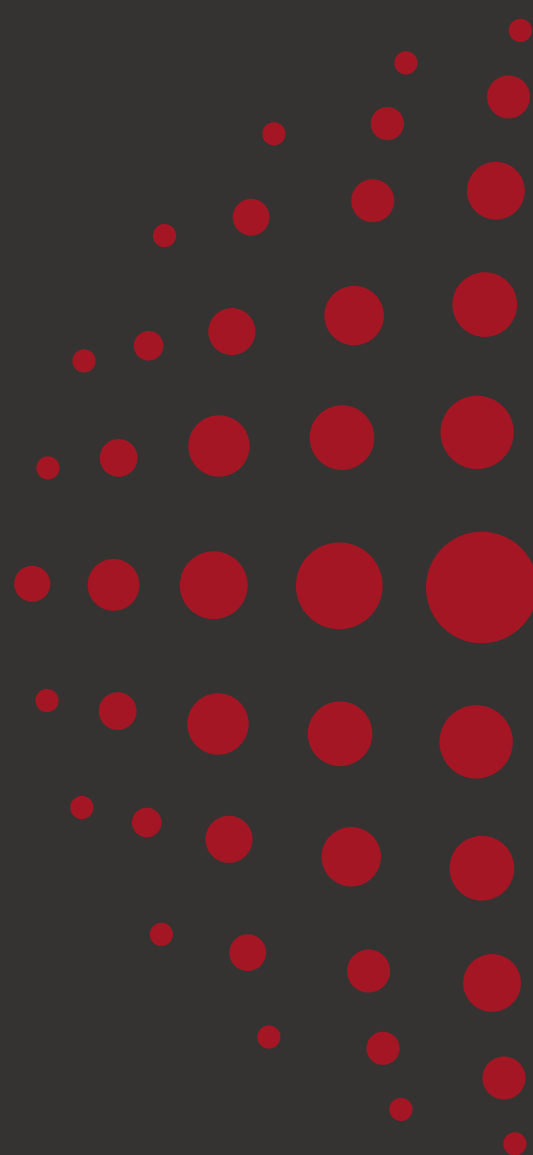
VII. CONCLUSION

In the days of economic crisis, stiffening the employment relationship should not take place. On the contrary, introduction of regulations making this relationship flexible is justified both socially and economically.

Until that happens, the tendency to supplant contracts of employment by civil law contracts, which are more favourable for employers, will become the norm and understandably so. One cannot disregard the fact that when it comes to choosing the basis for employment, the decision-making entity is mainly employers. An employee wanting to take up employment, especially at the outset of his career, has very limited potential for negotiation or does not have it at all.

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PORTUGAL

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I. OVERVIEW

a. Introduction

The distinction between employees and independent contractors (self-employment) may be pointed out as a recurrent issue discussed in numerous labour lawsuits in Portugal. This phenomena is a result of the fact that Portuguese labour law includes statutory provisions, a number of which are of a protective nature, that are applicable to employees, but not to independent contractors.

A special judicial procedure was introduced in Portugal in September 2013, with the purpose of reducing the possibility of companies and organisations imposing independent contractor hiring alternatives on job candidates, as a way to elude the application of statutory labour law principles and rules. The procedure is triggered by the initiative of the labour authority, when, on the basis of inspective visits to companies and other employers, cases of independent contracting (formally speaking) are found, which materially, adopt features that are typical to employment. The judicial procedure is filed and defended by public prosecutors in labour courts without the need for the interested independent contractor/employee confirming his or her interest in pursuing the lawsuit.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

According to the Portuguese Labour Code, employment comprises the commitment of an individual to provide manual or intellectual activity to an employer (company, organization or individual), against payment of an agreed salary and under the employer's supervision and direction, this being materialised on the employer's power to give orders to the employee, on the way to perform the work. In independent contracting, the provider undertakes to render a certain result through his or her manual or intellectual work and is not subject to the counterparty's power to give orders that is found in the employment type relationships.

Legal subordination (the power to give binding orders) is pointed out as being the decisive criterion to draw the line between employment relationships and independent contracting (self-employment). Nevertheless, in view of the difficulty to distinguish, in practical terms, cases that should qualify as one or the other, case law and authors have elected typical factors, which suggest the existence of subordination. The most relevant are:

- working time fixed by the beneficiary of the activity (the presumed employer);
- work being provided in a specific place determined by the presumed employer;
- the use of working tools provided by same presumed employer;
- payments being made on a periodical or regular basis (particularly fixed amount payments);
- the shaping of the work performance being based on regular orders and instructions from the presumed employer; and
- integration of the presumed employee/independent contractor in the presumed employer's organisation (or production) structure.

Additionally, when two of the abovementioned factors are met, there is a legal presumption that the case should be qualified as employment (even if the provider is formally presented as an independent contractor) meaning that in a specific lawsuit, the burden of proof on the qualification of the case as an independent contractor relationship will fall upon the presumed employer.

b. General Differences in Tax Treatment

Social security

Employers, employees and independent contractors are, in general, subject to contributions for the Social Security system, although there are separate rules and systems for employees, on the one hand, and independent contractor on the other. The amount of contributions is calculated on the basis of the gross amount or the salary or fees received.

In the case of employment relationships, the social security contribution rate is 34,75% (of the employee's monthly gross salary). 23,75% is borne by the employer and 11% by the employee (being deducted by the employer from the employee's monthly salary, upon payment). In case of non-profit organizations, the employer's rate is reduced to 22,3%.

In the case of independent contractors, social security contributions are due and fully borne by the independent contractor and calculated at the rate of 29,6% of fees received, although there are some special regimes subject to different contribution rates.

When 80% or more of a given independent contractor annual turnover (fees) are paid by the same entity, or group of entities, and such annual fees are equal to or exceed 2.515,32 €, the same entity is subject to an annual social security contribution equal to 5% of the annual fees it paid to the independent contractor.

There are a few specific cases where independent contractors are exempt from paying contributions to social security. These include cases of independent contractors that:

- accumulate self-employment with employment, provided that the following conditions are met:
 - the activities are separately provided to different entities that do not belong to the same company group;
 - the employment activity is subject to social security contributory system that includes all the social protection covered by the social security system applicable of independent contractors;
 - the amount of the monthly average salary covered by such social security system is equal to a minimum monthly value of 421,32 € which is a reference amount fixed annually as a social support index (IAS).
- are simultaneously pensioners, within the cases where professional activity can be legally cumulated with payment of pension allowances;
- during the previous year have paid contributions over an annual income amount that does not exceed 2.527,92 € (which is six times the amount of the social support index - IAS).

Tax

In all cases and as a rule, tax withholdings must be made over amounts paid to the employee and to the individual independent contractors although the rates depend, in the case of the employees, on a specific table that takes into account both the monthly income and the employee's family situation.

Services provided by independent contractors are generally subject to VAT (Value Added Tax). In some cases, however, services rendered by independent contractors are VAT exempt, that being the case for example, of independent contractors whose yearly turnover of taxable income does not exceed 10.000 € or in the case of specific activities connected with medical services, education, or arts and culture.

c. Differences in Benefit Entitlement

With the exception of the requirement to pay social security when the fees paid by a specific company or company group represents 80% or more of the independent contractor's annual turnover, there are no mandatory benefit entitlements for independent contractors.

Contrarily, employee benefits include paid holiday leave of at least 22 working days and special allowances such as vacation and Christmas allowances (of an annual amount, in both cases, roughly equivalent to one month's pay). Other leaves, such as marriage leave, maternity and paternity leaves and some authorised absences for family care, are also granted by law to employees. Collective bargaining agreements usually include other benefits such as meal and transport allowances, school allowances for employee children, seniority bonuses and in some cases, complementary pension plans or other social benefits.

d. Differences in Protection from Termination

Employees benefit from robust protections against contract termination considering that, as a rule, employees are not granted discretionary contract termination rights (the exception being termination during an initial probation period. Terms for the probation period vary between 15 and 240 days, according to the type of activity and the nature of the agreement; for average permanent employment contracts, the probation period duration is limited to a maximum of 90 days). Temporary contract duration agreements are also restricted to cases legally grounded on temporary company needs or on specific legal provisions that expressly allow temporary engagement and these are restricted. Therefore, termination upon contractually agreed duration is also limited to legally allowed cases.

Additionally, the employer is only allowed to terminate the contract in case of (a) mutually agreed termination; (b) dismissal for disciplinary grounds subject to prior internal dismissal disciplinary procedure; (c) individual or collective dismissal (for economical, structural or technological reasons), subject to an internal procedure and prior notice periods, which depend on the seniority of the employees affected by dismissal; (d) dismissal grounded on the employee's failure to adapt to the position, subject to specific and detailed pre-requisites.

Lawful dismissal for disciplinary reasons is limited to cases where the employee commits a serious offense that makes it unreasonable for the employer to keep the employment relationship (just cause). The following cases are examples of just cause under Portuguese law, provided they are sufficiently serious (or their consequences are sufficiently severe) to make it unreasonable, in practical terms, to maintain the existing employment relationship: (i) illegitimate disobedience to lawful orders received from the superiors; (ii) breach of rights and guarantees of other employees; (iii) repeated conflict provocation with other employees; (iv) repeated lack of interest in performing duties that are part of the job role, with the required level of care; (v) serious material damages caused to the employer; (vi) untrue statements in absence of justification; (vii) unjustified absence from work causing direct damage or serious risks to the employer (this being presumed as such, if the number of unjustified absences in any calendar year reaches five successive or ten interrupted absences); (viii) intentional non-compliance with health and safety rules at work; (ix) physical violence, insults or other offences punishable by law, committed at the workplace in relation to other employees, members of corporate bodies or the individual employer not belonging to such bodies or his delegates or representatives; (x) kidnapping and in general all crimes against freedom of those persons referred to above; (xi) breach or refusal to comply with court or administrative decisions and acts; (xii) critical productivity reduction.

In these cases, dismissal depends on the employer organising a formal (non-judicial) disciplinary proceeding, subject to strict formalities and to time limits. As a rule, proceedings must be initiated within 60 days upon the employer becoming aware of the infraction and, in any case, within one year as from the moment the infraction took place (unless the behaviour also qualifies as a criminal offence, in which case, the criminal law statute of limitations period, if longer than one year, will apply).

Individual or collective dismissal is also admitted when based on objective grounds. These are restricted to economical, structural or technological grounds and may consist of market grounds understood as a reduction in the employer's activity, caused by a decrease in demand for its goods or services or the impossibility, whether legal or practical, of placing those goods or services in the market. The employer's economical or financial imbalance, a change to its business activity, the restructuring of the business organisation or the replacement of the employer's main products may qualify as structural grounds. Technological grounds relate to changes in production techniques, automation of production tools, computerization of services or automation of means of communication.

Redundancy on objective grounds is subject to a formal internal procedure that must be initiated by the employer, which involves employee representative structures and may also involve the labour authority observers. Strict notice periods also apply, including a prior notice for the final dismissal communication to be effective, which, depending on the affected employee's seniority, varies between 15 (employees that have been with the employer for less than one year) and 75 days (employees whose seniority is equal to or exceeds 10 years).

Severance compensation in cases of individual or collective dismissal (for economical, structural or technological reasons) as well as in dismissal grounded on the employee's failure to adapt to the position, is based on a calculation that takes into account the affected employee's seniority and remuneration.

Pregnant employees, those that have given birth in the previous 120 days and those breastfeeding, as well as any employee on paternity leave, enjoy special protection against contract termination. Dismissal of any of these categories of employees is illegal without a prior favourable opinion from the competent authority in the area of equality of opportunities between men and women. If the authority states an unfavourable opinion, the employer may only proceed with dismissal of the protected employees through a court decision, recognising the existence of a valid motive in a lawsuit, that may be filed up to thirty days after the unfavourable opinion has been issued.

In contrast, independent contractors who are self-employed do not benefit from specific legal protection against termination and the parties are free to agree upon the termination conditions in the contract.

Nevertheless, if an independent contractor is dismissed and he/she believes that the contractual relationship materially qualifies as an employment agreement, a lawsuit may be filed in the labour courts, within the year immediately following termination, to assess the nature of the former contractual relationship and assess, under such light, its termination by the company.

e. Local Limitations on Use of Independent Contractors

In Portugal, there are limitations on the use of independent contractors as such. Nevertheless, there are, as referred to above, measures that envisage to excluding companies from engaging and keeping employees at their service agreements that, formally, are qualified as independent contracting.

f. Other Ramifications of Classification

Strict health and safety provisions at work directly benefit employees and are, generally, not required in the case of independent contractors.

Working time limitations and minimum rest period provisions also apply in the case of employees. Generally, working hour limits are set at eight hours a day and forty hours a week, although collective bargaining agreements very frequently include shorter working hours. There are a number of flexibility instruments that in some cases depend on an agreement between employer and employee and sometimes on collective bargaining agreements. In all cases, nevertheless, certain maximum limits apply. Additionally, the employer must keep an accurate work time registration system that allows the labour authorities to check the work performed, per employee, per day.

No mandatory working time restrictions apply to independent contractors.

There are two work compensation funds, which employers must contribute towards monthly, with 1% of remunerations paid to employees engaged after October 2013. These funds aim at guaranteeing that employees receive at least 50% of mandatory severance compensation payments.

g. Leased or Seconded Employees

As a principle, under Portuguese law, employers are prevented from assigning employees to other entities, in terms that allow the recipient entities to exercise authority and supervision powers over the employees, whilst the assigning employer keeps the employment contractual relationship with the original employee.

One of the allowed exceptions to the above mentioned principle is that of temporary agency work (temping agencies) holding the required license to temporarily assign workforce to third parties in exchange for remuneration, as a main business activity. Other than being additionally allowed to provide employee selection, orientation and professional training services as well as services in the areas of human resources management and consultancy, temping agencies are not allowed to provide other services. In Portugal, there are two types of temporary agreements between an employee and a temporary work agency (temping agency): a fixed-term temporary agreement and an open-ended temporary agreement.

The agreement entered into between a user company and a temporary work agency is of a temporary nature. This is the agreement under which the employee is leased by the temporary work agency to the user company in need of workforce.

The temporary agency work is therefore based on a triangle type relationship involving two different contracts and three entities. The triangle comprises two separate (but frequently connected) contracts: (i) a labour relationship between the temping agency and the temporary work employee; and (ii) a service agreement (a workforce lease agreement to be more precise) between the temping agency and the user company, by which the first agrees to assign its temporary work employee(s) to the latter. There is no direct contractual relationship between the user and the temporary work employee. Temporary workforce lease agreements can only be entered into in specific cases, connected with temporary company workforce needs, such as for temporarily filling-in vacant employment positions during a recruitment process or for replacement of employees that are off on sick leave or that, for any other reason, are temporarily away from work. Other cases in which temporary workforce lease agreements are admitted are cases where additional workforce is required to respond to temporary activity fluctuations or company intermittent workforce needs, or cases where the

implementation of specific limited duration company projects are at stake.

Specifically, the cases under which the use of temporary agency work is allowed are the following: (i) direct or indirect replacement of an employee who is temporarily absent; (ii) direct or indirect replacement of an employee with a pending lawsuit against the company challenging dismissal (and requesting reinstatement in the job); (iii) direct or indirect replacement of an employee on unpaid leave; (iv) direct or indirect replacement of a full-time employee temporarily providing part-time work; (v) seasonal activity workforce needs; (vi) exceptional temporary increase of the company activities; (vii) workforce required to execute an occasional task or defined and non-lasting service; (viii) vacant job position, during the respective recruitment process; (ix) intermittent manpower requirements resulting from activity fluctuations during days or part of days, provided the use of temporary work does not exceed half of the users standard weekly working hours; (x) replacement of employees that are subject to intermittent absence periods to provide direct family support, of a social nature, for days or part of days; (xi) workforce requirements in temporary projects.

Apart from tempting agencies, the other possibility for temporary employee assignment is an employee assignment between affiliated companies or entities sharing common structures. Employee assignment in these cases is limited to a maximum period of five years.

In these cases, assignment is possible provided the following requisites are met: (i) the assigned employee is a permanent employee of the assigning company; (ii) the assignment is agreed between affiliated companies (or companies that share common organization structures or means); (iii) the employee agrees to the assignment; (iv) the assignment is agreed for fixed periods (e.g. one year) that may be automatically renewable up to a maximum of five years; (v) the assignment agreement is made in writing.

h. Regulations of the Different Categories of Contracts

Employment contracts are subject to the provisions of the Portuguese Labour Code and some specific labour and social security legal acts. In a number of cases, collective bargaining agreements agreed between unions and either companies or company associations also apply to unionised employees and employers that have executed such agreements or that belong to the relevant employer associations. In a number of cases, companies agree to extend the collective agreement provisions to non-unionised employees and in a number of cases, government decisions extend the provisions of collective bargaining agreements to a whole business activity or economic sector of activity, either on a restricted geography or to all of the Portuguese territory. These provisions, regulating employment relationships, do not apply to independent contractors.

The Portuguese Civil Code contains provisions on service agreements that specifically apply to independent contracting and, as a rule, these are not restrictive or mandatory provisions, but mostly subsidiary provisions that apply when the parties have not provided for differently, in the contractual document.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

Factors that suggest the existence of a real contract of employment can be found in the Portuguese labour code as well as in several judicial decisions.

Despite the contract designation or qualification given by the parties, being that of an independent contractor agreement, the same may be re-characterized by the Portuguese labour courts, as being an employee relationship based on the actual terms under which it is performed.

As briefly referred above, Portuguese law defines an employment agreement as a contract in which a person assumes the obligation, in exchange for remuneration, to render work to another person, under the latter's authority and instructions. In contrast, an independent contractor is considered to provide a certain result of an intellectual or manual activity.

Three essential elements are to be found in an employment contractual relationship: (1) the rendering of an activity, (2) in exchange for remuneration, and (3) under the authority and instructions of the employer.

Subordination is an inherent feature of employment (which is not found in independent contractors) and understood as the legal situation of one who is subject to the orders and instructions given by another, with respect to the carrying out of a certain task. The activity is not self-determined as it is in the case of an independent contractor.

Examples of factors that have been found by courts to suggest, or to indirectly reveal subordination, may be found in features such as:

- i) who determinates the period during which the activity is to be performed;
- ii) who determines the place where the activity is performed;
- iii) whether there is periodical or regular fee or remuneration payment;
- iv) whether remuneration is based on time spent as opposed to other criteria;
- v) who organises or owns the means and tools needed to carry out the activity;
- vi) whether contractual bond is of durable or stable nature throughout a significant period of time;
- vii) what type of orders and indications are provided by the beneficiary to the activity renderer;
- viii) whether the activity renderer is included in the production chain of the beneficiary (e.g. whether he/she is subject to any sort of hierarchy chain-type of organisation);
- ix) whether all of the provider's fees come from one service beneficiary (being economically dependent of such beneficiary).

Finally, as mentioned above, the Portuguese Labour Code contains a legal presumption that an employment relationship is in place if at least two of the following features are found:

- the place of activity is either at the premises of its (the activity's) beneficiary or determined by it;
- work tools and equipment belong to the beneficiary;
- the provider follows a timetable determined by the beneficiary;
- the provider is paid a fixed (or guaranteed) amount based on a certain periodicity;
- the provider executes management or supervision functions within the beneficiary's organization.

Should any of these features be present, the burden of proof that the relationship is not an employment one is borne by the company.

b. The Legal Consequences of a Re-Characterisation

Hiring employees involves costs and burdens that some companies sometimes try to prevent by resorting to outsourced solutions and service agreement alternatives. Sometimes, nevertheless, these are then structured, in practical terms as actual employment relationships. Re-characterization may occur either as a result from an inspective visit or control from the labour authority targeted at a specific situation, entity or activity sector or when the individual personally raises the issue and claims recognition as employee. This is usually connected with cases where independent contractors claim employee protection against dismissal from labour courts.

When re-characterization is obtained from the court, social security proceedings are also usually initiated to obtain retroactive pay of social security contributions from the employer. As a rule, the employer will have to pay the employee's part of the contribution to the social security services (and deal with the right to claim the amount directly from the employee).

Additionally, the company may have to adhere to the Work Compensation Fund and to the Work Guarantee Compensation Fund (and be subject to pay an additional 1%), which may be due retroactively and the employer will have to contract a work accidents insurance and comply, in general terms, with existing obligations in terms of health and safety at work.

In the event that the independent contractor agreement is deemed to qualify as an employment contract, the employee is entitled to all credits arising from a subordinated relationship, such as paid holidays, Christmas and holidays allowances, meal allowance (if this payment is set forth in an applicable collective bargaining agreement), and others that may be foreseen in an applicable collective bargaining agreement.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Persons seeking "employee" status may address the competent labour court by lodging a declaratory action and if the court declares that an employment relationship is in force. In cases where the special lawsuit for re-characterization is initiated (by initiative of the public prosecutor based on the inspective activity of the labour authority), the court is also required to fix the specific point of time in the past when the employment relationship is deemed to have started.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Re-characterization also usually gives place to administrative infringements and fines being applied to the employers.

Companies resorting to independent contractor agreements in conditions that justify re-characterization, qualify as a very serious misdemeanour, punishable with the payment of a fine, varying between € 2,040 and € 9,690. Companies in a relation of reciprocal ownership, control or group, as well as the company directors may be jointly liable for the payment of the fine.

In case of recidivism, the company may be deprived from the right to receive benefits or allowances granted by public service or entities, for a period up to 2 years.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Under Portuguese law, there are no formal requirements to conclude a service agreement (agreement with independent contractor), although written form is recommended for purposes of evidence. In addition, all documents suitable as proof for the status of independent contractor (such as invoices, declarations, contractor's marketing activities, etc.) should be collected.

Regardless of which status the parties have chosen at the moment of the conclusion of the contract, the decisive criterion is how the contractual relationship is exercised on the day-to-day business. Thus, the abovementioned factors, which suggest the existence of an "employee" status, should be avoided both in the contractually agreed conditions and in practice.

b. Day-to-Day Management of the Relationship

In the day-to-day management of the contractual relationship, the independent contractor shall be treated as such and not with signs of subordination.

Periodical reviews of how the relationship with independent contractors is evolving should also be made to ensure that the de facto situation is not changing into an employment type relationship and should continue to be adequately characterized as an independent contractor agreement.

V. TRENDS AND SPECIFIC CASES

As referred, a special judicial procedure has been in force for over three years now in Portugal aimed at repressing the misuse of the independent contractor options, as a way of gaining full flexibility and cost reduction with the workforce component in businesses. A number of procedural issues have been discussed in courts around the provisions that govern these special procedures, considering that there was no judicial precedent for the type of judicial proceeding wherein, the independent contractor may actually choose not to even intervene in the lawsuit and trial, that may cause a contractual relationship of which he is a party to be re-qualified. Different understandings on whether the interests at stake in such lawsuits were limited to the directly interested party's interests (and therefore, on whether settlements confirming the independent nature of the relationship were allowed, as they would be in a normal declaratory lawsuit initiated by the independent contractor against the company) or, if on the contrary, such lawsuits involved public interest issues, and settlements between the parties on the contract qualification were restricted to the possibility of agreeing on its qualification as an employment agreement. The tendency of high court decisions was one point of consideration that the procedure entails public interest issues.

Attempts to launch legislative proposals to broaden the scope of this type of judicial measures, namely to other types of contractual structures and to public entity recruitment have been prepared, but seem not to have collected sufficient consensus to proceed, and to be proposed and discussed further.

VI. CONCLUSION

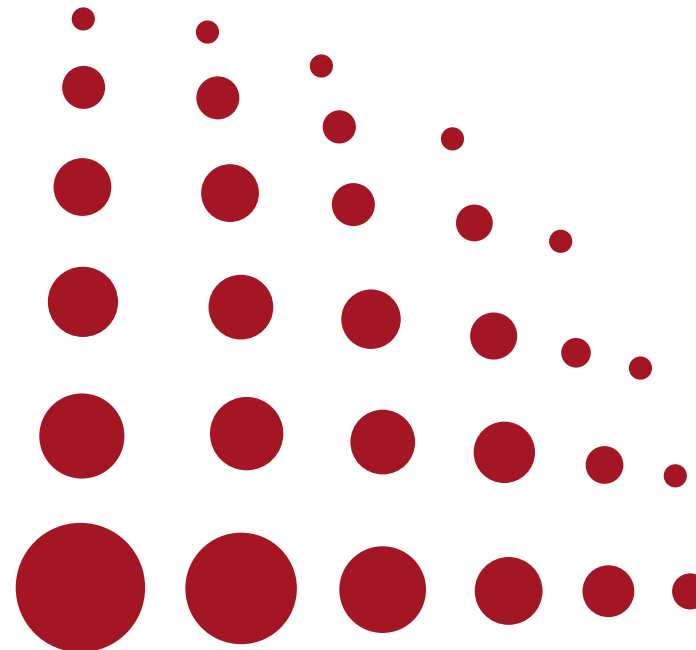
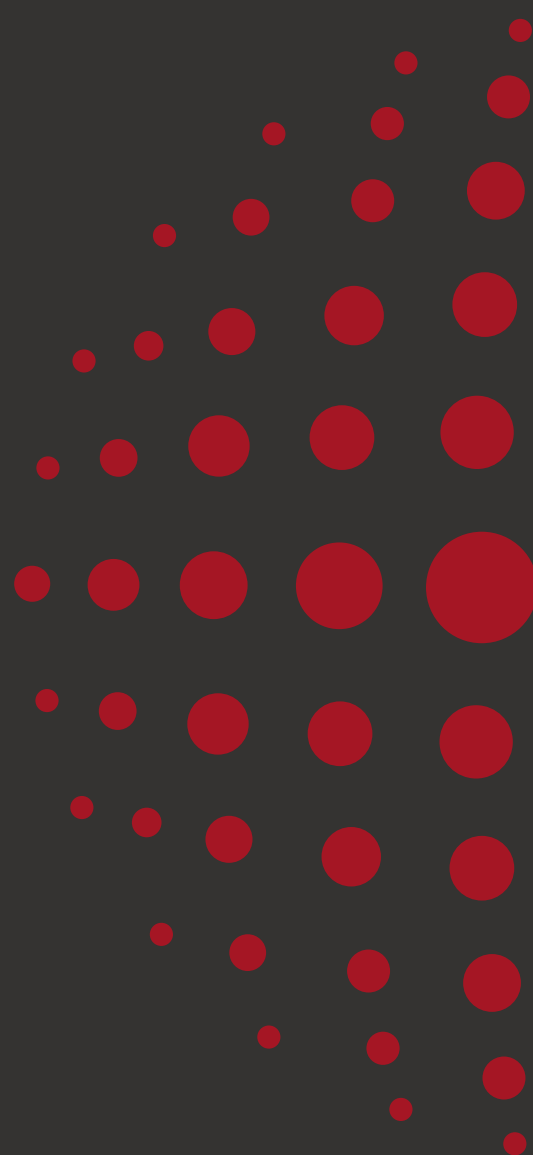
Companies are not limited in their choice to develop part of their activity on the basis of outsourced independent contracting solutions. The option to do this or to resort to

a structure based on employee teams and organisation should be taken on the basis of the type of activity that the company is looking for. Whether it is focused on the availability of the workforce (more typical to resorting to employees) where the company controls and governs the organisational and production structure, as well as the means that it considers should be applied to the activity or, on the contrary, is more focused on obtaining the results of the activity developed and organized by other entities. Nevertheless, considering the legal mechanisms that allow for re-qualification and the consequences of such re-qualification, resorting to employees disguised as independent contractors is not an advisable option.

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ROMANIA

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I. OVERVIEW

a. Introduction

A clear understanding of the distinction between the legal notions of Contractor and Employee is important in order to ensure that the right tax regime is applied to the two distinct legal relationships under the Romanian Law, but also in order to establish what type of benefits an individual is entitled to, or the type of protection that an individual can legally claim. In Romania the distinction has its roots in the Fiscal Code that was the first normative act that recognized the need for providing legal guidelines in determining what type of legal relationship an individual receives income from.

The possibility of re-characterization of a legal relationship, as being an employment relationship, has been recognized by Romanian courts. Individuals have claimed that they performed activity that should be considered as employment and national courts have recognized the existence of employment relationships even in the absence of employment contracts.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The Romanian Fiscal Code provides for legal definitions for **Dependent Activities** -

“any kind of activity performed by individuals during an employment relationship that generates income”

- and **Independent Activities** -

“any kind of activity performed by individuals in order to obtain income, that meets at least four of the following criteria:

3.1. the individual has the freedom of choice of where and how he performs his activity and the program for the activity;

3.2. the individual has the freedom to perform activity for more than one customer;

3.3. risks inherent to the activity are assumed by the individual who performs the activity;

3.4. the activity is performed by using the patrimony of the individual that performs the activity;

3.5. the activity is performed by the individual through use of his intellectual and/or physical performance, depending on the specific activity;

3.6. the individual is part of part of a professional body/professional order that has representation regulatory and supervision rights over the profession conducted under special regulations governing the organization and the exercise of the profession in question;

3.7. the individual has the freedom to conduct his activity directly by hiring personnel or in collaboration with third parties, according to legal provisions”

The new legal definitions were introduced in the new Fiscal Code that became applicable in 2016 and are a result of the confusion of the old legal definitions that were unclear created. As a result of being regulated as distinct activities by tax law they have different legal regimes and they are submitted to different tax regimes.

Dependent activities, meaning those arising from an employment relationship, are subject to special regulations of employment law, while independent activities carried out by individual contractors are - as a rule - subject to the general provisions of civil law. In order to perform dependent activities an individual employment contract between employer and employee must be concluded according to the Romanian Labour Code, while independent activities are provided on the basis of civil contracts concluded in the general conditions stipulated by the Romanian Civil Code. Also, as a result of the new definition of independent activities, the legal provision clearly states that they can be performed on the basis of specific professional contracts such as legal assistance contracts specific to the lawyers.

Individual employment contracts are extensively regulated by the Romanian Labour Code, which provides a framework of strict rules on the conclusion, enforcement, amendment, suspension and termination of such contracts, while independent activities can be provided by individual contractors under a variety of civil contracts, some of which enjoy a special regulation in the Romanian Civil Code - such as the mandate contract, others just observing common rules stated in the Romanian Civil Code. Romanian legislation does not regulate a special contract under which the independent activities are carried out. However, indirect legal provisions and common language, use the general term of "service providing contracts" when referring to the legal basis on which independent activities are provided by individuals.

Employment status is acquired by individuals only by entering into an individual employment contract that must be concluded in writing in order to be valid. The individual employment contract must be registered in the electronic records of regional institutions that monitor and control the correct application of employment law, prior to the beginning of the dependent activity. The existence of an individual employment contract validly concluded is what distinguishes the legal status of employees to the legal status of individual contractors. Even the criteria introduced by the new legal definition for the independent activities point to the fact that they have to be analyzed while taking into consideration the content of the contracts the individuals conduct in order to perform the specific activity.

Both individual employment contract and civil contracts, under which independent activities are provided by individuals, are subject to the general principle of mutual consent involving an agreement between the two contracting parties – the individual providing the activity, both dependent and independent, and the beneficiary. However, for the employment contract there are minimal legal limitations under which the parties cannot negotiate certain terms, such as the guaranteed minimum wage or the minimum number of days of annual leave enjoyed by employees, while in civil contracts there can be negotiated clauses without restrictions other than those imposed by general civil legislation on prohibited clauses in any type of civil contract - such as the prohibition for the inclusion of clauses that are a fraud under the law, or immoral clauses. For specific independent professions there can also be legal provisions on the minimum content of the contracts, but usually the clauses that are mandatory are different from the ones in the employment contracts. From the existence of these general restrictions arises a discussion on the simulation of an employment relationship by concluding a civil contract, in order to avoid the legal limitation imposed by employment law. In these cases, the re-characterization of the civil contract as an individual employment contract and the establishment of the existence of a simulation must be made by the court.

In order to limit these attempts to avoid the legal limitation imposed by employment law, individual contractors that provide independent activities are subject to prior authorization under strict regulations. In case of concluding contracts with unauthorized individuals that provide activities for a beneficiary we can find the premises for unlawfully receiving individuals for work, a conduct sanctioned as a contravention or exceptionally even as a criminal offence according to national law.

In fact, the only legal definition of the individual contractor generated by transposing Directive 89/391/EEC into national law by Government Decision No. 300/2006, referring to the work performed on permanent or temporary sites, it qualifies them as "any person authorized to carry out a professional activity independently and assume contractual duty to the beneficiary ... to achieve ... works for which he is authorized".

A separate category of individuals that provide independent activities for a beneficiary is those of the liberal professionals or freelancers – for example health professionals, lawyers, notaries, experts, mediators, etc. Usually these professions have independent regulations and they are organized according to their own statutes. Given the fact that each liberal profession is exercised under different conditions, for each of them a regime was regulated for the registration, authorization, effective performance of work, membership of professional bodies, their contributions under pension schemes, the possibility to provide the specific activity under the liberal profession status or as an employee (as in the medical staff case). The liberal professionals usually provide their activity on the basis of a collaboration contract regulated by the same statutes.

The employees are conducting their activity in a subordinated relationship with the employer, while the individual contractor is engaged in a civil legal relationship with the beneficiary of the activity, which is characterized by the equality of the parties. Employees carry out their work for the benefit of the employer who assumes the risks of the activity performed for him, while the independent contractor bears the risk of the contract under common law and criteria that distinguishes the independent activities from the dependent activities.

Regarding the remuneration of the activity provided, the employee is legally entitled to receive a salary for his work, while the individual contractor will negotiate the remuneration for the activity that he performed. A special mention must be made of the fact that the work performed under a full-time individual employment contract is entitled to a minimum compensation for the employees established by government decision – i.e. a minimum gross salary per economy guaranteed for payment. A lower remuneration of an employee cannot be settled upon, even if both parties agree. On the other hand, individual contractors do not receive a guaranteed minimum income, even in the situation in which they are providing an activity comparable to full-time employment. For some independent activities legal provisions establish minimum limits for the remuneration of at least part of the individual contractor's activities.

b. General Differences in Tax Treatment

As noted at the beginning of this analysis, the tax treatment of the two categories of individuals providing dependent or independent activity is regulated differently. Regarding income tax, whether the income is a result of a dependent activity based on an individual employment contract or the income is a result of an independent activity provided by an individual contractor, the Romanian fiscal system establishes a unique 16% income tax regime that differs in the way in which the income tax is withheld and remitted by the two categories of individuals. Thus, for employees the 16% income tax is calculated, withheld and paid to the tax authorities by employers, while independent contractors must declare income subject to income tax, owing advance payment of income tax or final payments of income tax, according to the tax treatment of their choice.

Regarding social contributions for the employment relationship, they are paid jointly by the employee and the employer the latter having the obligation to calculate, withhold and remit both the employee quota and an additional quota owed by him for the use of employee labor. As for the individual contractors, they are required to pay social security contributions in a direct, declarative system. Efforts have been made in order to equalize the quotas owed by the employees and the individual contractors. For the individuals providing either independent or dependent activity, social rates of contributions are aligned, with the additional quotas being paid by the employer for the use of employee labor. Given the fact that the employer has to pay additional social contributions for each employee, the cost of the activity performed is higher for employers than for the beneficiaries of the activities performed by the independent contractors. It is also one of the main reasons why beneficiaries requiring the work of individuals choose to contract under the civil law rather than establishing an employment relationship.

Regarding persons exercising liberal professions, most of these professions have organized their own pension systems, and professionals are no longer required to contribute to the public pension system. However, a special situation arose with notaries who established their own pension system, but still have the existing obligation to contribute to the public pension system. There are also liberal professions for which there is no organized personal pension system; these professionals are contributing to the public pension system, usually by conducting a contract with the entitled authority.

c. Differences in Benefit Entitlement

Contributing to the medical system in equal ways, both the employees and the individual contractors are medically insured, meaning that they will receive equal treatment in the public medical system (free emergency treatment, low payments in case of hospitalization, compensations for certain type of medication etc.). However, individual contractors will not benefit from paid medical leave, since this is a compensation that is recognized only for employees.

Both employees and individual contractors benefit from parental (maternal and/or paternal) leave compensation according to their previous income, with the exception of the medical maternal leave that is also recognized only for female employees.

Employees only benefit from unemployment compensations on termination of employment and from incentives provided by the Government in order to encourage them to find work outside their geographical area or to relocate. Compensations and active measures after collective dismissals are recognized only for employees.

Employees contribute and benefit from the national public pension system, while individual contractors can contribute and benefit from the national pension system if they conduct a contract with the entitled authority. As stated, some professions have a distinct pension system and the professionals will contribute and benefit from that distinct pension system.

Social protection measures for employees are recognized by law. These measures include employees' health and safety, working conditions for women and young people, establishing a minimum gross salary per economy, weekends, paid annual leave, work performed in special conditions, training, and other specific situations. This general recognition of social protection rights has its basis in the constitutional regulation, regulations governing each of these issues being alternatively established. Individual contractors do not enjoy legal protection on these rights and will negotiate in accordance with the principle of mutual consent the conditions under which they will provide their activities.

Though both the employment contract and civil contracts under which the individual contractors provide their activities involve a negotiation between the parties, for the individual employment contract, the Romanian Labour Code provides a number of essential clauses to be necessarily included in all the contracts, while the content of civil contracts under which individual contractors perform independent activities is not regulated.

An important aspect for the activities performed by employees is that the working program is regulated and a number of rests periods and benefits for working overtime are guaranteed. Also, there are strict regulations on work performed during the night and work performed during the holidays. For the individual contractors these rights are not guaranteed, so there are no laws regulating their daily rest, their weekly rest, overtime rewarded with time off or extra pay, just as there are no rules in place for the activity conducted during the night or during holidays. This situation may open the possibility of abuses committed by beneficiaries of the independent activities that may require the contractors to work on short deadlines or require an amount of activity that forces the independent contractor to work continuously for a long period of time. Not benefiting from the legal protection of these minimum rights, individual contractors must negotiate civil contracts in such a manner as to avoid taking an excessive workload for a short period of time, or accepting tasks that imply working extensively by night time without proper rest time.

Another legally recognized right for employees is the right to paid leave. The Romanian Labor Code establishes a minimum number of days of annual leave that employees may benefit from for their work, with the possibility of negotiating a greater number of days of annual leave by individual negotiation, or collective negotiation, at each employer's level, while usually independent contractors are paid only for the time they perform the independent activity. Usually civil contracts are concluded for a determined period of time, or for a specific campaign and have no provisions on periods of time in which the contractors are paid the specified amount of money for that period without any activity being conducted during the specific period – similar to a paid leave. As for the right of sick leave, as stated even if the independent contractors are contributing to the public health system, there are no regulations stating the conditions in which the contractors may not perform the activities they were contracted for by the beneficiary due to health reasons. Independent contractors do not benefit from paid sick leave, but can negotiate clauses with the beneficiary on this matter.

d. Differences in Protection from Termination

There are differences in the legal treatment in case of termination of the two types of contracts - individual employment contracts and civil contracts under which the independent contractor provides activities for a beneficiary. The termination of the contracts by mutual consent of the two parties is always possible in both types of contracts. Even in this case, there is a special rule for the individual employment contract stating that in the event of mutual agreement on termination of contract the employee has to be the one who asks the employer for termination of the employment relationship, while in civil contracts termination by mutual consent may be requested by either party.

Regarding the termination of contracts by individual initiative of the person providing the activity for a beneficiary, the employees have the legally recognized right to resign, subject to a notice period that benefits the employer. There are legal provisions stating the maximum notice period, but notice periods can be negotiated to a lower level. As for the individual contractors they can denounce a civil contract only in accordance with the common law as long as they negotiated the possibility of unilateral termination of the contract. Considering the activity provided by an independent contractor as having a

successive character in accordance with the Romanian Civil Code, in case of termination of the civil contract at the contractor's initiative, he must provide a "reasonable" notice, in the absence of express contractual provisions on this matter.

The most significant differences in the two types of contract termination can be observed in the case of termination of the contracts by the initiative of the beneficiary. The beneficiary may initiate termination of the civil contract, in a similar, symmetrical way that the individual contractors providing independent activities can, according to common law, or to the negotiated provisions of the civil contract, with a reasonable notice period as previously mentioned. As for the employer, it may take the initiative of the individual employment termination for his employees only in the cases stated by the Romanian Labor Code. Thus, the employer may dismiss his employees for reasons regarding the employee's person, if the employee has committed a serious disciplinary offense, if he is subject to preventive arrest or house arrest for a period exceeding 30 days, or is found to have a physical and/or mental inability to perform specific work activities as well as in the case of professional unfitness of the employee. The employer may also dismiss employees for reasons not related to the employee's person in case of motivated dissolution of the work position, in which case the dismissal can be individual or collective. Termination of the individual employment contract by the employer in situations other than those covered by the Romanian Labor Code is not possible.

Another important issue related to the termination of contracts by the initiative of the beneficiary is the handling of disputes that may arise from abusive denunciation. Thus independent contractors, if they consider that the beneficiary has abusively terminated the civil contract, can only use actions based on common law and such disputes fall under the jurisdiction of judges that handle general civil litigation. As being submitted to common law, most of these disputes are assigned to lower courts, under the criteria of the value of the matter. As for the dismissed employees, the Romanian Labor Code provides a separate section on control and punishment of unlawful dismissals. As a result of these special provisions, the annulment of dismissal measures fall under the jurisdiction of specialized judges at higher courts. There are also special rules of procedure regarding labor disputes, including overturning the legal burden of proof, so that the employer is the one that must prove the legality and validity of the dismissal, even if the claim comes from the employee. These exceptions to common law are a consequence of the subordination relationship between employer and employee, which generates the need for additional protections to employees that are considered to be at a disadvantage.

Regarding the restoration of the anterior situation – *restitutio in integrum*, as a result of a court ruling finding the unfairness of termination by the employer, the employee is provided with the legal right to be reintegrated and the right to receive damages equal to the wage indexed, actualized and updated and all other rights to which he would have received if he had not been dismissed, while for the independent contractors only common law provisions apply in terms of damages.

The labor law provides a number of special cases of rightful termination of the individual employment contract, while civil contracts follow the common law rules for the rightful termination of contracts. Some cases of rightful termination of contracts operate in both individual employment contracts and civil contracts, such as the occurrence of the death of the individual provider of the activity – employee or independent contractor, or the death of the beneficiary – if the beneficiary is an individual, or the completion of the period for which the contract was concluded. On the other hand, there are some special cases of rightful termination of the individual employment contract, cases that do not apply to civil contracts. One such case is the rightful termination of the individual employment contract, in the event of a simultaneous fulfillment of standard age and minimum period of contribution conditions in the public pension system. While independent contractors contribute – as a rule – to the public pension system, the civil contracts under which

they provide their activities do not terminate on the simultaneous fulfillment of the two conditions for retirement. Independent contractors are entitled to pension on demand, and the retirement does not have any effect on the existence of the civil contract. For certain categories of professionals – such as lawyers – that contribute to their own pension system, if they retire under their statute provisions, they no longer have the right to fully practice their profession.

Rules on collective dismissal and the protection of individuals in case of collective dismissal only apply to employees. This is the case, not only because the legal provisions provide the legal frame only for the employees, but also because the individual contractors negotiate and conclude civil contract on their own not as a collectivity of professionals providing a specific activity.

e. Local Limitations on Use of Independent Contractors

In some specific industries and also in the public services there are some limitations in the use of independent contractors for specific activities. For example, in ports operations the employers can only use the work of employees that are subject to specific registration and authorization at the port's authorities. Also in public services the public institution can only use the work of public servants (employees with a special Statute) or employees for the main activity, with the possibility of contracting under civil law only for specific areas, such as lawyers for legal matters.

f. Other Ramifications of Classification

Some of the independent professions have special Statutes that limit the activity of the professionals to only one type of activity. For example, a lawyer as an independent professional cannot perform work under an employment contract (aside from a few exceptions, such as teaching activities in universities). That is not the case for the employees that can usually perform work (without limitations on what kind of activity they perform) for more than one employer without limitations (unless the employee agrees to an exclusivity clause).

g. Leased or Seconded Employees

In the case of leased or seconded employees there is no direct contract between the beneficiary of the activity and the employees, meaning that the employees don't conduct civil contract with the beneficiary. A contractual relationship exists between the initial employer and the beneficiary, while the employees continue the employment with the initial employer.

Individual contractors have the liberty to conduct civil contracts with any beneficiary meaning that they will have contractual agreements with all the beneficiaries. Individual contractors cannot be leased or seconded since they are not subordinated to any of their contractual partners.

h. Regulations of the Different Categories of Contracts

As stated for the employment contract there are legal provisions on the minimum content and the form of such contract. Parties must negotiate at least the minimum clauses as stated by law having the possibility to add additional clauses according to their negotiation. For the civil contracts there are only few general rules that apply, giving the parties a wider range of possibilities when negotiating such contracts. For some specific independent professions there are regulated contracts that independent professionals need to use.

An alternative for beneficiaries who do not want to enter individual employment contracts or civil contracts directly with independent contractors, is entering into the so-called "service providing contracts" with other entities that will provide personnel to the beneficiary. The personnel provided will not gain the employee status at the beneficiary company and will not be in any contractual agreement directly with the beneficiary. In such case, there is no direct contractual relationship established between the beneficiary of the work performed and individuals that will perform the work. A direct contractual relationship is established between the beneficiary and the entity that provides the personnel. The staff is paid by the entity that provides the personnel, while the beneficiary pays any negotiated amounts for the services provided by the entity. In such cases, the entity that provides personnel can be an employer for the leased employees, or just an intermediary for legally authorized individuals that will perform their activities for the beneficiary the intermediary chooses and in the terms the intermediary negotiates for them.

The work is performed by the personnel on behalf of the beneficiary, but in case the activities are not conducted as stated in the contract or requested by the beneficiary, being the fact that there is no contractual relationship between the beneficiary and the personnel that performs the activities, there is no direct action against the personnel, instead the beneficiary has a direct action against the entity that provides the personnel.

The personnel not being hired by the beneficiary, the latter is not bound by specific legal provisions of labor law, but by the contractual provisions that were negotiated with the entity, which provided the personnel and the general provisions of civil law common to all contractual relationships. If the personnel is employed by the entity that contracted with the beneficiary, all special labor law provisions will apply between the personnel and their employer.

In some areas, however, to avoid the use of under-qualified personnel for work under special conditions and in important fields that require rendering tasks with a high degree of risk by individuals who may not enjoy the special protection of employees, legal provisions prohibit service providing contracts for the activities the beneficiary is legally authorized to perform.

As stated earlier, civil contracts under which individual contractors provide independent activities and the service providing contracts between the beneficiary and an entity that provides personnel do not enjoy independent regulation under Romanian legislation so that they are governed by common law rules.

For those aspects regarding individual employment contracts and employment relationships in general, not specifically regulated by labor law, the rules of common law will be used as well, as a result of the fact that the employment contract is a variety of civil contracts. This being the case, in some situations the distinction between an individual employment contract and a civil contract tends to be very subtle and the correct characterization of the contract by the court can be required.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

There are no legal provisions that regulate the re-characterization of independent contractors as employees, the individuals that want their activity to be recognized as employment being able to address the court on general procedural rules on the recognition of a state of facts. In order to determine if a contract is an employment contract the courts need to analyze the existence of 3 cumulative criteria – the purpose

of the contract is performing work; there is remuneration for the work performed in a form of a salary and the employee is subordinated to the employer during the performing of the activity. The last criteria, is the one that distinguishes between the existence of an employment contract and a civil contract.

b. The Legal Consequences of a Re-Characterisation

As mentioned previously, entering into civil contracts with individuals that are not authorized to perform the activity stated in the contract, or entering into a civil contract with an individual that is authorized, but under similar conditions as an individual employment contract, can be qualified as unlawfully receiving individuals for work, a conduct sanctioned by law.

A legal qualification of a civil contract as being an individual employment contract is usually an attribute of the courts, which are usually referred to by independent contractors that provide activities in conditions similar to an individual employment contract, but do not enjoy specific protection legally recognized for employees. Another situation that may occur is that of questioning the type of contract that exists between the individual and the beneficiary by the local labor inspection bodies. Following such an inspection, these local bodies can ascertain that the activities provided by the independent contractors are specific to typical work activities performed by employees, without the existence of a legally concluded individual employment contract.

In this case the beneficiary will receive the sanction for unlawfully receiving individuals for work, which is equivalent to a re-characterization of the legal relationship between the parties, but in order to achieve the effects of the recognition of the labour relationship between the parties, the court must make a ruling for every individual case. Thus, although the labour inspection bodies ascertain that the activities provided by the independent contractors are specific to typical work activities performed by employees for the period in which the activities were conducted under a civil contract, the contractors are not automatically granted specific rights of employees and are not provided with specific protections for the employees, unless they obtain a court ruling stating so.

The beneficiary that unlawfully receives individuals for work without perfecting an individual employment contract is sanctioned progressively, his action being a contravention – if the number of individuals he receives for work without perfecting an individual employment contract is under 5, or a criminal offense punishable under the Romanian Labour Code and general rules of criminal law, if the number is higher than 5.

Regarding the activities performed by individuals exercising specific liberal professions, if the re-characterization of their cooperation contracts as individual employment contracts by the court is not possible, being the fact that these professionals cannot achieve the employee status.

The differences in legal status between individuals having the employee status and the independent contractor status under the Romanian legislation caused by the under-regulation of civil contracts, under which individual contractors perform their independent activities, can lead to situations in which beneficiaries will use different types of contracts that suit their purposes without a proper protection for the individuals providing the independent activities. In order to avoid this, a better legal frame is needed.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

As stated, the individual seeking the recognition of his employee status needs to address the court in order to achieve this recognition and to benefit from the specific statute of an employee. The court can recognize the employee status even after the contractual

agreement, or the performing of the activity has ended, as the Supreme Court stated in a binding general ruling. After the recognition of the employee status, the individual can benefit from special protection specific to employees (for example in case of unfair dismissal) and can claim employee specific entitlements (for example paid vacation periods, or seniority bonuses).

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Apart from the rights that the individual was entitled to as a result of achieving the employee status by the re-characterization of his contractual relationship, he can also claim financial damages if he can prove that by not having the employment relationship being recognized from the beginning of his activity he suffered damages that cannot be covered by any measure and need to be compensated in a financial matter. The individual has to state the amount and prove that the damages are as high as the amount that he claims.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

In order to avoid the confusion between a civil professional relationship and an employment relationship the most important thing is having a clear contract between the individual performing the independent activity and the beneficiary. The contract has to clearly state that the individual contractor is not subordinated when performing the specific activity for the beneficiary, this being a major issue in analyzing the relationship between the two parties.

Also for tax purposes, the parties need to properly document the fact that in performing the independent activity the individual meets at least 4 of the 7 criteria stated in the legal definition of independent activities. Also the individual has to keep financial and tax records according to legal provisions.

As stated previously, there are only a few rules in concluding a valid civil contract, but this does not mean that finding a proper form for such a contract is an easy thing. The Romanian Civil Code states that in every area that a special type of contract is regulated, special rules stated for that contract must apply. So a valid civil contract between the beneficiary and an independent contractor does not have to allow for the possibility of the re-interpretation of the contract as being a special type of contract – in this case an employment contract.

This distinction must also apply to the activities conducted for the beneficiary – meaning that the activities conducted by independent contractors usually are not activities with a permanent and constant character and are different from the current activities that employees are conducting for the beneficiary.

The control over the activities conducted by the independent contractor is circumscribed to the contractual provisions, meaning that every disagreement regarding the activities conducted must be settled according to these contractual provisions or in court.

b. Day-to-Day Management of the Relationship

In the day-to-day operations the individual performing independent activities for the beneficiary has to remain independent, meaning that the beneficiary can only use

contractual clauses in order to control the way the individual performs the activity and cannot interfere in the way the individual performs the activity. The beneficiary cannot issue orders for the independent contractor and cannot directly sanction the independent contractor for the way he performs the activity (with the exception of any existing sanction clauses that need to be constructed in a way that ensures the independence of the individual performing the activity).

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

In some specific industries (such as the IT) there has been a decrease in the number of civil contracts being conducted, most companies using employees due to the special tax regime that the industry enjoys (no income tax for revenues generated by the IT industry). On the other hand, some other industries such as financial management and legal services tend to rely more and more on civil contracts.

The differences in tax regime are less evident according to new regulations meaning that in the next period the use of independent contractors as a way to avoid a higher level of taxation will decrease.

One common practice in Romania is as described above the temporary use of employed force to provide services to another company than the employer, meaning that the employer hires a number of individuals with specific qualifications that he uses to provide services to other companies. In this case the individuals are always employees and not individual contractors, being subordinated to their employer and not to the company that they are providing their service for. This has become the main way the companies avoid paying higher wages to their own employees, by contracting services at lower rates than the combined wages that they would have paid if they had used the employed force. The employees used in providing the services to the company are paid by their employer lower wages than the employees of the company they are performing services for. At this moment this is a legal business conduct.

b. Recent Amendments to the Law

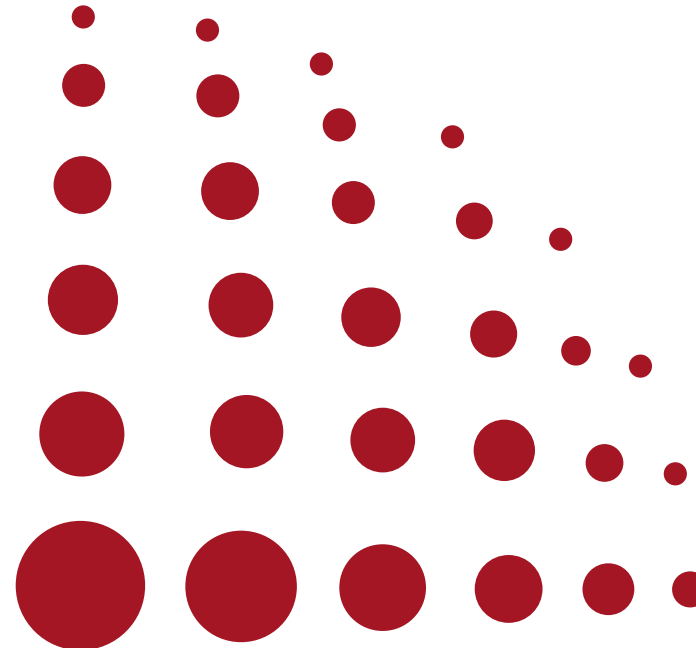
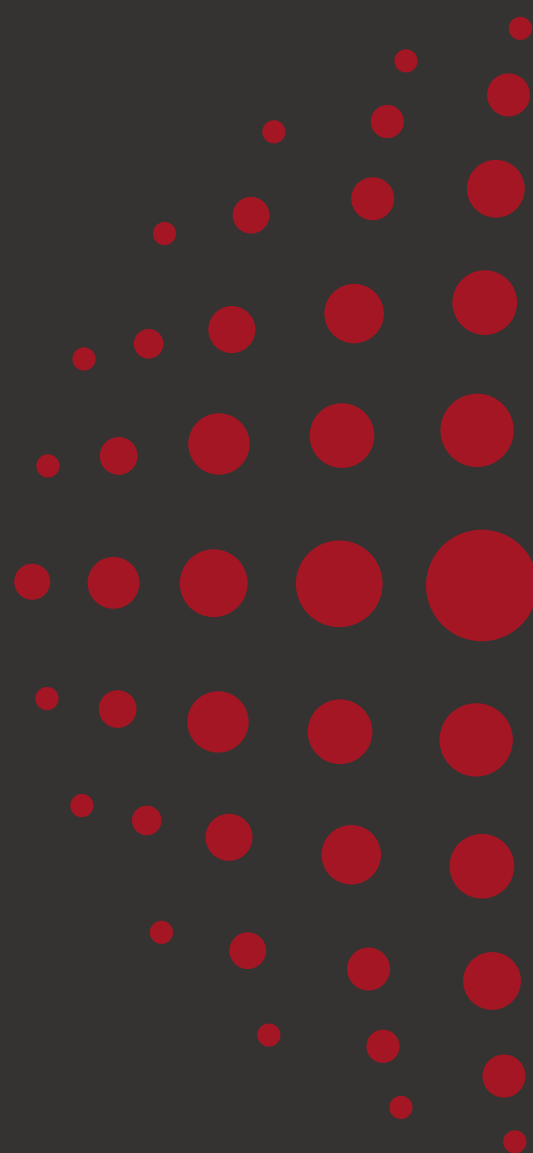
As mentioned, starting 2016 the Tax Code has introduced new legal definitions for dependent and independent activities in order to ensure a more clear distinction between the two notions. The Government has put efforts into constructing a more balanced tax regime for each of the two categories of activities in order to avoid the use of civil contracts for activities that usually have to be performed by employees. However there are still no specific legal provisions on the re-characterization of independent contractors as employees, this being an issue that still needs to be addressed.

VI. CONCLUSION

The differences in legal status between individuals having the employee status and the independent contractor status under the Romanian legislation caused by the under-regulation of civil contracts, under which individual contractors perform their independent activities, can still lead to situations in which beneficiaries will use different types of contracts that suit their purposes without proper protection for the individuals providing the independent activities.

Such situations are a source of inequity that the law does not yet sanction. In order to prevent such inequities there have been steps made in improving legal provisions in order to have a better distinction between the dependent and independent activities. However the legal frame has to be extended in order to regulate the so-called service providing contracts that are still used in a way that can generate inequities for the individuals.

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SERBIA

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I. OVERVIEW

a. Introduction

The issue of re-characterisation of an independent contractor into an employee seems to be increasingly topical in Serbia as more domestic and foreign companies (especially in the IT sector) look for flexible forms of engagement. This is not necessarily to by-pass the rigid and expensive employment regime but often because the contractors prefer working outside the employment arrangements to allow greater independence (e.g. the possibility to work flexible hours and to develop their business by providing services to multiple companies).

When it comes to re-characterisation of the contractual relationship, Serbian court practice is still quite scarce. There are only about a dozen relevant court decisions, none of which specifically address the issue of re-classification of an entrepreneur working under a service agreement, which is probably the most commonly used type of engagement outside employment among IT and consultancy companies. The court practice mostly relates to blatant cases of clandestine work, such as when an individual holds no agreement at all with the employer, or has an agreement for work outside employment, which is clearly a sham (e.g. constant engagement under out-of-employment agreements designed for seasonal work).

Currently, the risk of re-classification is commonly perceived as being low to moderate.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

According to the Serbian Labour Act, an *employee* is an individual holding an employment agreement with an employer. An Employer can be either a domestic or a foreign legal entity or individual. An *employment relationship* is normally established by an employee entering into an employment agreement with the employer. The Labour Act requires the employment agreement to be concluded prior to the commencement of work, in written form, and prescribes its mandatory elements. The Labour Act also sets the minimum employee rights (such as daily and weekly rests, vacation entitlement, working time limitations, minimum salary, mandatory allowances, conditions and procedure for termination of employment, notice period, protection of certain employee categories).

The law provides for several types of contractual relationships other than employment, the most widespread of which is a service agreement. An employer can engage an individual under a service agreement only for the performance of work that falls outside the scope of the employer's business activities. Apart from the requirement that a service agreement is to be made in a written form, the Labour Act is silent on the terms of a service agreement. The minimum guarantees that apply to employees do not extend to individuals working under a service agreement. The parties to a service agreement are largely free to stipulate the terms of engagement, including the remuneration amount, and a notice period in case of unilateral termination. The Obligations Act prescribes the general terms of a service agreement, which apply to the extent the parties have not agreed otherwise.

Employers, especially those in the consultancy and IT sector, mostly use a service agreement (often called a 'consultancy agreement') for engaging individuals registered as entrepreneurs. The terms 'contractor', 'self-employed person', or 'freelancer' are widely used to refer to an entrepreneur. The Companies' Act defines the entrepre-

neur as a natural person who is registered in the public register for performing certain business activities. It is relatively easy for an individual to register as an entrepreneur. An entrepreneur is liable with all his assets for the obligations stemming from the performance of business activities.

The Labour Act recognises employment even in the absence of a written employment agreement, by prescribing that if an individual commenced working at an employer without an employment agreement in place (or a genuine agreement outside employment), it shall be deemed that he established an on-going employment relationship with that employer. This notion is known as 'factual employment'. Also, a non-genuine agreement for work outside employment can be deemed as an employment agreement, by applying the general rule of the Obligations Act on the nullity of the simulated agreement and the validity of the concealed (dissimulated) agreement instead (provided that the conditions for the existence of the concealed agreement are fulfilled).

The law does not explicitly prescribe the set of qualities that allow for re-classification. When delineating employment from out-of-employment status, the courts tend to take into account the presence of the qualities of an employment relationship stemming from the Labour Act, in particular the following:

- whether the activities fall within the scope of the employer's business activities. The limited scope of activities allowed under a service agreement is the main point of difference between an employment relationship and engagement under a service agreement. The risk from reclassification is higher if the employer already has employees who work on the same or similar tasks as the contractor, or if the work performed by the contractor can be subsumed by a role existing at the employer;
- whether there is a strong relation of subordination, such as a requirement to obey the day-to-day instructions of the employer;
- whether the contractor enjoys the employee rights provided by the law (such as a fixed monthly remuneration, fixed working hours, increased pay for overtime, salary compensation during vacation and sick leave, holidays, mandatory allowances), and/or does he benefit from the rights that the employer provides to its regular employees (e.g. working tools, use of company email, a company car, fringe benefits);
- whether the employee is employed elsewhere on a full-time basis. The Labour Act prescribes that an employee may concurrently work at multiple employers, provided that his total working hours do not exceed the full-time hours. If the employee works full-time elsewhere, the courts would probably see it as an obstacle for recognising additional employment;
- whether the contractor is subject to the same rules of conduct as the employees of the particular employer (e.g. whether the employer's code of conduct applies to the contractor);
- whether there is a requirement for the contractor to provide the services personally, i.e. without the possibility of subcontracting;
- whether the contractor's work is continuous and extends over an unlimited period of time, rather than being a one-off engagement (e.g. for creating or repairing a specific item), or project-based work; and
- whether the contractor undertook to work exclusively for the employee.

A single employer engaging a substantial number of individuals outside employment can be perceived by the authorities as unusual, especially given that Serbian law and practice traditionally treat employment as the basic form of engagement. The relevant authorities' can therefore become suspicious in that situation as to whether the nature of the relationship between the employer and the contractors is genuine. Another situation, which can invite suspicion from the relevant authorities, is where the contractor

regularly works in the employer's offices.

Engaging an individual who is registered as an entrepreneur (versus an individual who is not registered as an entrepreneur) does not safeguard an employer from the risk of the engagement being found to be (concealed) employment. This is because the notion of being an entrepreneur does not represent a separate entity from the individual registered as an entrepreneur.

When it comes to the assessment of employment vs. out-of-employment relationship by administrative authorities (i.e. the labour inspectorate and the Tax Authorities), the employer's legal presence in Serbia can be relevant. If a foreign company has no presence in Serbia in the form of a subsidiary, a branch or a representative office, the labour inspectorate and/or the Tax authorities will most likely not consider that company as an employer with the capacity to enter into an employment contract governed by Serbian law. This follows from an official opinion of the Serbian Ministry of Labour, which stated that an individual cannot conclude an employment agreement with a foreign-based company which is not registered in Serbia (through a branch/representative office), because the individual would be unable to enjoy all the rights stemming from mandatory social security. Although it can be argued that this opinion is not in accordance with the Labour Act (because the Labour Act prescribes the possibility of foreign-based legal entities and natural persons to engage individuals based on employment agreements for working in Serbia), and although the obstacle related to social security is technical in nature, the labour inspectorate and the Tax Authorities are likely to follow the Ministry's opinion. Unlike these authorities, the court is less likely to consider the Ministry's opinion as authoritative, and is instead more likely to rely on its independent interpretation of the Labour Act.

b. General Differences in Tax Treatment

The differences in tax and social security obligations can differ significantly depending on the type of engagement entered into by the parties.

In an employment relationship, the employer is obliged to calculate, pay and withhold: salary tax, at a flat rate of 10% and social security contributions at a total rate of 37.8%. The mandatory social security contributions go towards pension and disability insurance, health insurance, and unemployment insurance. The Social Security Contributions Act provides the maximum amount for social security contributions to be five times the average salary in Serbia. If the income generated by an employee exceeds the maximum amount, social security contributions are payable on the maximum only with the income exceeding the maximum is subject to salary tax only.

The same salary tax rate and social security contributions rates (10% and 37.8%, respectively) apply to an independent contractor who is registered as an entrepreneur. The main difference between the taxation of the two categories comes from the possibility for the independent contractor to be in the lump-sum taxation regime. If the Tax Authorities accept the entrepreneur's application for lump-sum taxation, the Tax Authorities will determine the base for his tax and social security liability by using various criteria, such as the type of business, the average monthly salary in Serbia or the relevant municipality, the market conditions for performing the business activity, the location of premises, and the entrepreneurs age. Given the lengthy criteria and the lack of consistency in its application by the Tax Authorities across the country, it is difficult to provide an accurate assessment of tax base in the lump-sum taxation regime.

The lump-sum taxation model is the most popular taxation option among freelancers. Under the lump-sum taxation regime, the entrepreneur's tax and social security base is determined in a fixed amount, which is usually much lower than it would be if he was

employed. This enables the entrepreneur to take home more money than he would as an employee, especially if his remuneration is significantly higher than the average salary in Serbia.

An entrepreneur is eligible to apply for the lump-sum taxation if:

- his annual turnover (in the year preceding the year for which tax is determined, or the expected turnover at the start-up of the business) is not higher than RSD 6,000,000 (approx. EUR 48,400);
- he does not operate in one of the following businesses: accounting; bookkeeping; audit; tax advising; marketing; market research; wholesale; retail; hospitality (hotels and restaurants operation); financial mediation; and business related to real estate;
- he is not registered as a value added tax payer, in accordance with the applicable regulations; and
- he does not receive investments from others.

c. Differences in Benefit Entitlement

The minimum rights provided by law to employees (such as working time limitations, minimum salary, leaves and rests, paid vacation, paid sick leave, etc.) does not apply to contractors, and the parties are free to agree on the terms of engagement. An independent contractor is typically only paid for the services he effectively rendered.

Below, we discuss the benefits that the independent contractors are typically concerned about when negotiating the engagement. Some employers stipulate full or partial coverage of these benefits, making them equal or similar to those granted to employees. This could contribute to the risk of re-classification, although so far the significance of providing these entitlements to contractors has not been tested in the context of re-classification.

Paid sick leave

For the first 30 days of sick leave, the employer is obliged to pay salary to the employee at the rate equivalent to 65% of the employee's average salary over the 12 months prior to the month in which the inability to work occurred ('reference salary') in case of sickness or injury unrelated to work. Where the employee suffered occupational disease or injury at work, the employer is obliged to pay the employee 100% of the reference salary. After 30 days, the compensation is funded by the state.

Maternity leave benefit

A female employee is entitled to pregnancy leave and childcare leave. Pregnancy leave starts no earlier than 45 days, and no later than 28 days, prior to the due date and lasts for three months from the childbirth. Childcare leave commences upon the expiry of the pregnancy leave. Pregnancy leave and childcare leave combined may last for up to 365 days (or up to two years in case of giving birth to a third (and every next) child). During pregnancy and childcare leave the employee is entitled to be paid an amount equivalent her average basic salary for the 12 months preceding the absence ('reference salary'), up to a maximum amount equivalent to five average salaries in Serbia. The employer is obliged to calculate and pay this to the employee, and can receive a refund of the equivalent amount from the state.

An independent contractor is also entitled to receive payment during pregnancy leave and childcare leave. The payment is calculated according to the same formula as for employees, the difference being that the contractor's basis for the calculation of this benefit is her base for social security contributions. If the contractor is in a lump-sum tax regime, the base for social security contributions is usually significantly lower than what the contractor's reference salary would be. Therefore, such contractor will receive a

lower amount during maternity leave than an employee with comparable gross earnings. Compensation for post-termination non-compete covenant

For employees, a non-compete clause can be stipulated in the employment agreement, with the post-termination non-compete limit being a maximum of two years. In order for the post-termination non-compete to be valid and enforceable, the employer must undertake in the employment agreement to pay the employee a specific compensation.

Conversely, a post-termination non-compete covenant stipulated in the contractor's service agreement is valid and enforceable even if the company does not pay compensation (provided that it is not excessive from a competition law aspect). This is under the assumption that the service agreement with a contractor is a genuine service agreement. If the service agreement would be re-characterised as employment agreement, the post-termination non-compete would be held unenforceable in the absence of special compensation for that period.

d. Differences in Protection from Termination

The differences in the possibility of terminating an independent contractor and an employee are significant. According to the law, an employer may unilaterally terminate an employee only if there is a valid reason. The possibilities for termination due to employee's misconduct are limited to the breaches prescribed by the Labour Act, the employer's general enactments, and/or the employment agreement. Other grounds include redundancy, committing a criminal offence in relation to work, and underperformance. The termination procedure is very formal. Although the Labour Act does not prescribe a mandatory notice period in case of unilateral termination (except in case of underperformance), the termination procedure is often lengthy (the duration depends on the circumstances of the particular case, and the pace of successfully delivering the termination documents to the employee in accordance with special rules).

An independent contractor may be terminated even without cause, if so stipulated in the agreement, with the obligation to observe any contractual notice period. In practice, termination of an independent contractor without cause is usually subject to a one-month notice period.

e. Local Limitations on Use of Independent Contractors

The Labour Act prescribes that a service agreement can be concluded for work, which does not fall within the engaging entity's business activities. Therefore, the type of the work performed by the independent contractor is a factor when determining whether the relationship with the independent contract is genuine. Other than that, in Serbia there are no other explicit limitations on the use of independent contractors.

f. Other Ramifications of Classification

A person engaged outside employment is not entitled by law to the minimum rights that the Labour Act grants to employees (such as working time limitations, minimum salary, leaves and rests, paid vacation, paid sick leave, etc.), and the parties are free to agree on the terms of engagement. There are certain rights however that apply equally to those engaged outside of employment as to employees including, the same mandatory occupational health and safety standards and protection from harassment in the workplace (mobbing) and anti-mobbing protection.

g. Leased or Seconded Employees

In March 2013, Serbia ratified the International Labour Organisation's (ILO) Private

Employment Agencies Convention (No. 181), committing to regulate staff leasing, and to enable the work of staffing agencies. However, staff leasing or temporary staffing have not been regulated in Serbia. Nevertheless, this type of engagement is quite common, and is tolerated in practice. There are several outsourcing companies in Serbia that provide staff leasing services. Still, staff leasing arrangements, because they are not regulated, entail a risk from recognition of an employment relationship between the leased individual and with the company, which is the beneficiary of staff leasing arrangements. A leased employee's claim for recognition of employment with the company for which he actually works could especially take place if the leased employee is dismissed as a result of terminating the business cooperation agreement between the staff leasing agency and the company that uses staffing services. Currently there is no relevant court practice, and the associated risks are considered remote.

h. Regulations of the Different Categories of Contracts

Serbian law defines several types of agreements outside employment:

- service agreement (elaborated in section II a.). This type of agreement is the most commonly used for engagement outside employment, and is used to engage individuals (usually independent contractors, i.e. entrepreneurs). The law does not prescribe different categories of this contract;
- agreement on temporary and occasional work, which can be concluded for the performance of work which by its nature lasts up to 120 working days in calendar year (e.g. seasonal work);
- agreement on vocational training, and agreement on vocational development, used for trainee work;
- agreement on additional work, for up to 1/3 of full-time working hours (this agreement can be concluded with employees engaged full time by another employer);
- voluntary work agreement (only with respect to non-for-profit activities); and
- management agreement (for engaging a company representative outside employment).

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

The Labour Act prescribes, that an employment relationship must be established by the employer and the employee, by entering into an employment agreement before employment commences. However, the Labour Act upholds the existence of an employment relationship even in the absence of a written employment agreement, by prescribing that if an individual commenced working at an employer without an employment agreement in place (or a genuine agreement outside employment), it shall be deemed that he established an indefinite-term employment relationship with that employer. This is known as 'factual employment'.

In addition, a sham agreement for work outside employment can be deemed as an employment agreement, by applying the general rule of the Obligations Act on the nullity of the sham agreement and the validity of the concealed agreement instead (provided that the conditions for the existence of the concealed agreement are fulfilled).

If a foreign company has no presence in Serbia in the form of a subsidiary, a branch or a representative office, the labour inspectorate and/or the Tax authorities will most likely not consider the foreign company as an employer with the capacity to enter into an employment agreement, and would therefore not re-characterise a contract. This follows

from an official opinion of the Serbian Ministry of Labour, according to which an individual cannot conclude an employment agreement with a foreign-based company, which has no legal presence in Serbia (as elaborated on in section II a. above). Tax Authorities and the labour inspectorate would likely follow the Ministry's opinion.

b. The Legal Consequences of a Re-Characterisation

The contractor can claim re-characterisation before the court. The contractor can claim the benefits pertaining to an employment relationship (e.g. increased pay for any overtime work and night work), which would have arisen in the three years before the re-characterisation.

Alternatively, if the labour inspectorate finds that the nature of the contractor's engagement resembles employment, it may order the employer to enter into an employment agreement with the contractor.

In addition, the Serbian Tax Authorities could determine, by applying the 'substance over form' principle, that the engagement of the contractor is to be treated (according to its economic substance) as employment for tax purposes. There is no established practice of the Tax Authorities as to re-classification of a contractor's relationship into an employment agreement, but the Tax Authorities would presumably rely on specific criteria (see section on General Differences in Tax Treatment). As a consequence, the Tax Authorities could consider the contractor's income as salary under an employment agreement and order the employer to pay the full amount of personal income tax and social security contributions that it should have paid on the salary. The statute of limitations for the tax audit is five years from 1 January of the year following the year when tax was due (the statute of limitations is paused by each action of the Tax Authorities related to a taxpayer in respect of assessing and collecting tax; Once the pause comes to an end, the statute of limitation period commences again and the time elapsed does not count).

The tax-related risks would be very remote if the engaging entity does not have a legal presence in Serbia. In that case, the entire burden of tax and social contribution payments is on the contractor, hence the contractor (and not the foreign entity) would be deemed liable. The law recognises the notion of 'secondary tax duty', according to which the entity that contributes to or assists the primary taxpayer (in this case, the contractor) in tax evasion is also liable for tax evasion. However, this has yet to be applied to a foreign entity in the context of re-classification.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Re-characterisation of a service agreement as an employment agreement is generally possible upon a claim for declaratory relief filed by the independent contractor.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The employer could be liable for a misdemeanour and subject to a fine of ranging from RSD 800,000 to RSD 2,000,000 (approx. EUR 6,450 to EUR 16,130). The responsible person at the employer could be fined from 50,000 to RSD 150,000 (approx. EUR 400 to EUR 1,200).

If the Tax Authorities were to classify a contractor relationship as employment, the employer can be found liable for a misdemeanour (failure to timely file the tax return, calculate, and pay taxes) and fined from 30% to 100% of the unpaid tax, the amount of the fine cannot be less than RSD 500,000 (approx. EUR 4,000) for a legal entity. In addition, the employer can be found liable for the criminal offence of tax evasion

(Serbian Criminal Code defines the tax evasion as intentional avoidance of payment of taxes, social security contributions and other statutory duties). The penalty for the criminal offence can be imprisonment of up to 10 years and a monetary fine.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

There are no required guidelines for documenting a contractor arrangement. The service agreement should clearly mention that the relationship is not an employment relationship, and the contents of the agreement should not resemble the features that are typical for an employment relationship. Terms such as 'salary', 'working time', 'overtime', 'vacation', should be avoided.

b. Day-to-Day Management of the Relationship

The limited case law concerning the issue of re-classification does not create a rich source of tips to reduce the risks when it comes to day-to-day management of the relationship with independent contractors. We think, however, that the following could help reduce the risks of re-classification to an absolute minimum:

- the work instructions should not be too detailed, as the contrary could indicate subordination. It is recommended to keep the work guidance general, e.g. what the final product should look like;
- employers should avoid fixed monthly payments as the method of remuneration. Alternatively, employers can pay the contractor upon the completed work, or per hours he actually worked and documented in a timesheet;
- the working hours should be as flexible as possible. Preferably, the start and the end of a working day should not be defined; and
- employer should avoid, to the extent possible, contractors performing work in the employer's premises, and/or using the employer's equipment and/or email account.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

So far, the authorities have not been vigorously awarding re-classification, nor have they been vigorously imposing the consequences of re-classification. However, this may change in the future. We are already noticing an increase in the number of court decisions being brought, and awarding re-classification, have been in the last couple of years.

b. Recent Amendments to the Law

It is expected that the Government will soon publish the first draft of the Staff Leasing Act (which, for the first time, will address this type of work in Serbia).

VI. CONCLUSION

In Serbia, the traditional employment relationship is still the predominant form of workforce engagement. Currently, the relevant court practice regarding re-classification is limited, and the authorities have not been vigorously inspecting or sanctioning

sham forms of contractor engagement. With the growing sectors that demand more flexible working arrangements (in particular IT and consultancy), we expect a growing trend of engaging independent contractors via service agreements. This could eventually lead to more reaction from the authorities, as they encounter more and more cases of flexible work engagements. Therefore, employers should be aware of the factors that can possibly contribute to re-classification, and of the consequences of an independent contractor being re-classified as an employee. The risk can be mitigated by properly structuring the relationship with independent contractors.

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SINGAPORE

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I. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Generally speaking, persons engaged under a ‘contract of service’ are considered to be employees, while persons who are engaged to work under a ‘contract for service’ are deemed to be independent contractors.

Whether an individual is an employee or an independent contractor is ultimately a question of fact. There is no single conclusive test, which may be used to distinguish between a ‘contract of service’, and a ‘contract for service’. Rather, the Courts will consider a variety of factors, such as:

Control

The element of control is an important function of the employer-employee relationship. An employer is expected to be able to exercise control over the work process, method and timing and is ultimately responsible for the provision of work.

An employee will be subject to the employer’s rules and regulations in the workplace and may be subject to disciplinary actions in the event they breach the employer’s rules. An independent contractor on the other hand will not be subject to such discipline.

Ownership of the tools or equipment used

Another indicative factor as to whether an employment relationship exists is whether the employer provides and maintains the tools or equipment used. In a contract of service, the employer typically provides the necessary tools and equipment, which are required for the work. By contrast, an independent contractor will generally have to provide his own equipment to perform the required services.

Method of remuneration

While not conclusive, the method of remuneration may also give an indication as to whether a contract of service exists between the two parties. An employee would more typically be remunerated on a regular basis (e.g. through a monthly salary) as opposed to being remunerated through commissions or lump sum payments.

Obligation to work solely for the employer

Consideration should also be given to whether the individual is required to work solely for the employer. An employment relationship is typically exclusive and an employee is expected to devote their time and attention within the work hours to their job. An independent contractor would typically have more freedom to choose what work they wish to do and can provide services to others.

Economic considerations

It may also be helpful to consider the economic considerations involved. If an individual is carrying out business on their own account, as opposed to for an employer, it is more likely they will be deemed an independent contractor.

Other pertinent questions on economic considerations include whether the individual shares in the profits or whether they are at risk for loss, and how earnings are calculated and profits derived.

b. General Differences in Tax Treatment

Central Provident Fund contributions

Employers in Singapore are responsible for paying contributions to the Singapore Central Provident Fund (“CPF”) in respect of employees who are Singapore citizens or Singapore

permanent residents. The CPF is a compulsory comprehensive savings plan for working Singapore citizens and Singapore permanent residents to fund their retirement, health-care and housing needs.

All eligible employees and their employers must make monthly contributions to the CPF. Contribution rates change periodically and are tiered based on the employee's age and whether the employee is in the private or the public sector. As of 1 January 2016, the maximum rates are 17% for the employer and 20% for the employee (of the employee's monthly salary capped at SGD 6,000). The contribution rates differ for employees in age brackets above 55.

An employee is taxed on their full employment income and no deduction may be made in respect of their personal expenses. An independent contractor however may treat their expenses as business expenditure and set off these expenses against their income, to lower their taxes.

c. Differences in Benefit Entitlement

The primary piece of employment legislation in Singapore is the Employment Act (Cap 91) of Singapore (the "Employment Act"). The Employment Act generally applies to all employees working under a contract of service with a Singapore employer, except for certain categories of employees (such as managers or executives with monthly basic salaries of more than SGD 4,500 and seafarers). Additionally, Part IV of the Employment Act (which covers rest days, hours of work etc.) only covers, amongst others, a non-workman (who is covered by the Employment Act) and earns a monthly basic salary of not more than SGD 2,500.

Employees who fall under the Employment Act (the "EA Employees"), enjoy certain minimum standards of employment and benefits. This includes annual leave, paid medical leave, public holiday pay and overtime pay.

In Singapore, independent contractors are not entitled to any specific employee benefits. Any benefits or remuneration due to them would be by way of contractual agreement under their 'contract for service'.

d. Differences in Protection from Termination

Employment contracts in Singapore are also subject to the general principles of contract law. Contracts of employment may be terminated by agreement, performance or expiry, frustration and repudiatory or fundamental breach.

Typically, such employment contracts include express provisions, which allow the employer or employee to terminate the contract of employment by giving notice, and the serving of a stipulated notice period.

Where a notice period has not been agreed between the employer and employee, certain statutorily prescribed periods apply to EA Employees. For instance, where an EA Employee has less than 26 weeks' service with the employer, the prescribed notice period would be one day, and if an EA Employee has at least five years' service, their notice period would be four weeks.

EA Employees may, if they believe they have been unfairly dismissed, appeal in writing to the Singapore Minister for Manpower, requesting to be reinstated. If their appeal is successful, the Minister may either order the employee's reinstatement to their former job or order a compensation payment.

Singapore has recently put in place a mandatory retrenchment notification. Employers who employ at least 10 employees must notify the Ministry of Manpower if five or more employees are retrenched within any six month period beginning 1 January 2017.

A contract for service (unless it is a fixed term) will usually have a termination clause with a stipulated notice period. Such a notice period tends to be shorter than notice periods agreed between an employer and employee. Independent contractors are not protected by any minimum statutory prescribed notice periods.

e. Local Limitations on Use of Independent Contractors

There are no local limitations on the use of independent contractors. There is however the risk that a person who has been contracted as an independent contractor may be construed as an employee. In that situation, there may be ancillary issues such as whether the employer has fulfilled its statutory duty to pay CPF contributions in respect of the individual. This situation is more likely to arise where the contract has been poorly drafted.

II. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

While the inclusion of express provisions setting out the relationship of the parties (e.g. being an employer-employee relationship, or an independent contractor) in the relevant contract or such other document, may be a relevant factor, it is not in itself conclusive as to the relationship, which exists between the parties.

Regardless of the characterization, which the parties themselves have imposed on their relationship, the Courts will look at substance over form. This basically means that the Courts will go beyond such express characterization accorded by the parties, and study the reality of the relationship as a question of fact, while bearing in mind the various factors discussed in Section I above.

Accordingly, the Courts may re-characterize a 'contract for service' into a 'contract of service', should sufficient factors indicate that the relationship is factually that of an employer and employee.

The burden of proof would typically be on the independent contractor (as plaintiff), who would need to demonstrate that he is an employee.

b. The Legal Consequences of a Re-Characterisation

Where an independent contractor has been re-characterized as an employee, a number of consequences may arise.

Firstly, the employer may be liable for additional statutory contributions under Singapore law. For instance, where the employee is a Singapore citizen or a Singapore permanent resident, the employer may be required to make the applicable contributions to the CPF of the employee, for the period of the employee's employment.

Secondly, the re-characterization of the independent contractor as an employee opens the employer up to vicarious liability issues. While the employer-entity is generally not vicariously liable for the actions of independent contractors, he would typically be vicariously liable for the actions of an employee carried out during the course of employment.

Additionally, should the re-characterized employee fall under the category of an EA Employee, he would be entitled to enjoy the relevant benefits provided pursuant to the Employment Act. As mentioned above, this may include annual leave, paid medical leave, public holiday pay and overtime pay. The employer may also be liable to the re-characterized employee, for additional compensation or benefits (over and above the express terms of his contract), which the employer grants to its regular employees. As an example, where the employer provides all its employees with pension fund contributions, or a non-discretionary bonus, the re-characterized employee may make an argument that he would be entitled to the same benefits.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

The person seeking ‘employee’ status may wish to bring an action against the employer-entity in court. Typically, this course of action would be undertaken only after negotiations with the employer-entity are unsuccessful.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The employer may be liable for the CPF contributions and the additional benefits raised in Section II.b above. Additionally, the employer may also be liable for certain fines which may arise for its failure to meet statutory obligations in respect of the employee (assuming the employee is an EA Employee), e.g. for a failure to issue key employment terms and itemized pay slips for the employee.

III. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

It would be prudent to document the independent contractor relationship by way of a written contract. This would enable both parties to delineate the boundaries of their relationship clearly and to set out the terms of the engagement.

It is recommended that the clauses do not indicate an employer-employee relationship by reference to the factors mentioned in Section I above. The parties should expressly state the independent nature of the independent contractor, and not include anything which might indicate a subordinate relationship, such as the independent contractor having to comply with regular working hours, the rules and regulations of the workplace and/or being subject to internal investigations and disciplinary processes.

b. Day-to-Day Management of the Relationship

When managing the relationship with the independent contractor, the party engaging the independent contractor may wish to avoid day-to-day management of the relationship.

While an employer is likely to be concerned about **work process**, the person who engages an independent contractor will focus on the **work product**.

IV. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

A foreign corporation, which carries on business in Singapore, must register a presence

in Singapore under the Companies Act (Cap 50) of Singapore. ‘Carrying on business’ is generally not defined but includes administering or managing, or otherwise dealing with, property situated in Singapore as an agent, legal personal representative, or a trustee, whether by employees or agents or others, and does not exclude activities carried on without a view to making a profit.

One of the factors considered in determining whether a non-resident person is carrying on business in Singapore is whether there is a permanent establishment in Singapore.

Section two of the Singapore Income Tax Act (Cap 134) of Singapore defines a “permanent establishment” as a fixed place where a business is wholly or partly carried on, including:

- a place of management;
- a branch;
- an office;
- a factory;
- a warehouse;
- a workshop;
- a farm or plantation;
- a mine, oil well, quarry or other place of extraction of natural resources;
- a building or work site; or
- a construction, installation or assembly project.

A person is deemed to have a permanent establishment in Singapore if that person:

- carries on supervisory activities in connection with a building or work site or a construction, installation or assembly project; or
- has another person acting on that person’s behalf in Singapore who:
 - has, and habitually exercises, authority to conclude contracts;
 - maintains a stock of goods or merchandise for the purposes of delivery on behalf of that person; or
 - habitually secures orders wholly, or almost wholly, for that person or for such other enterprises as are controlled by that person.

As such, if the independent contractor or contractors conduct themselves in the manner described above, it is likely that the foreign corporation engaging the independent contractor would be deemed to have a permanent establishment in Singapore and any income arising there will be subject to Singapore tax. A foreign corporation that fails to register properly and carries on trade or business in Singapore will be liable for penalties for non-registration.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

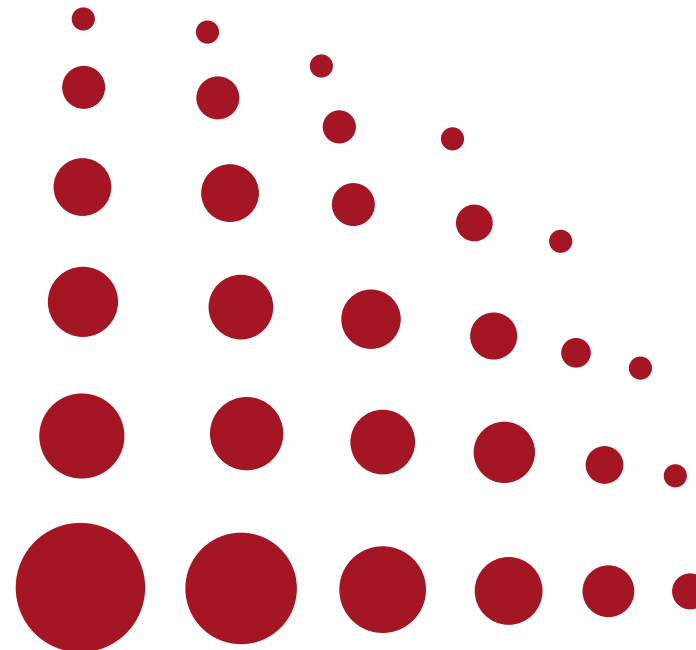
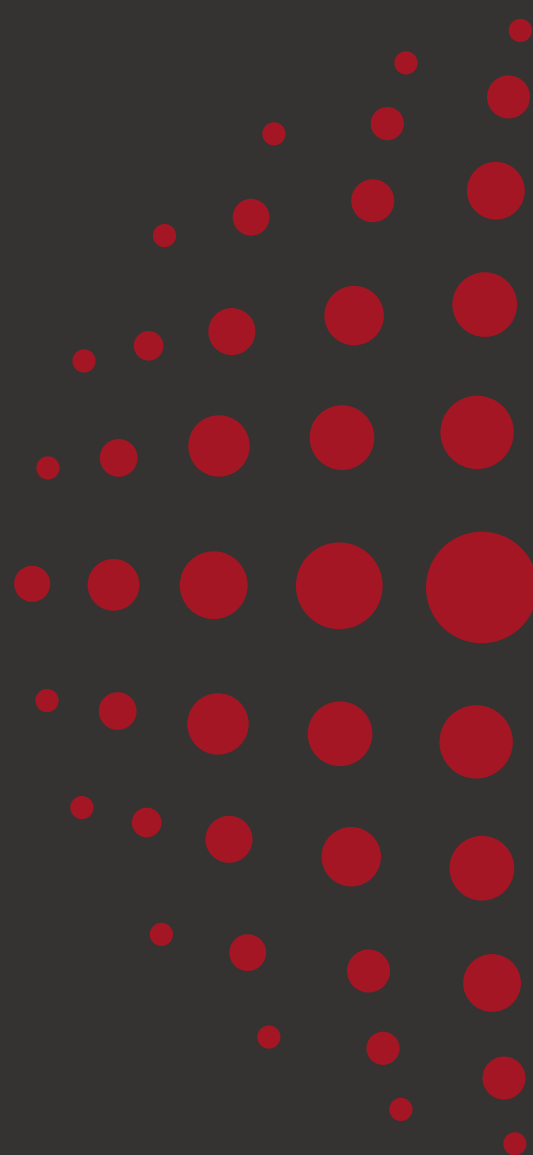
An employee does not perform their work in their personal capacity but on behalf of, or in the name, of the employer. As such, the employment of individuals in a country to provide services in the name of the employer is likely to create a permanent establishment risk and to expose the employer’s income to Singapore tax.

V. CONCLUSION

This chapter touches on the key distinctions between an employee and an independent contractor in Singapore. As there is no single test or factor which decisively determines whether an individual is engaged as an employee or an independent contractor, much

will depend on how the working relationship is defined in the contractual document and the implementation of that relationship. A carefully drafted contract and well-considered corporate structure or work process will go a long way in helping to avoid the risk of creating a permanent establishment and of exposure to statutory and compliance requirements in Singapore.

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SOUTH AFRICA

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I. OVERVIEW

a. Introduction

South African law has always recognised that independent contractors are distinct from employees and they remain excluded from the protections afforded to employees by the various statutory instruments enacted to regulate employment relationships. Recognising the dangers of trying to codify in legislation when a person will or will not qualify as an independent contractor rather than an employee, employment legislation in South Africa has largely avoided defining what an independent contractor is and it has been left to the courts to develop tests through jurisprudence to distinguish the nature of the relationship. The boundaries of what constitutes an independent contractor relationship have been pushed both by employers attracted by the perceived greater flexibility of an independent contractor relationship (and particularly the absence of the security of tenure protections – especially unfair dismissal protection - afforded to employees) and by individuals seeking greater freedom in how they work (and sometimes perceived income tax advantage). Exploitation of lower earning, more vulnerable individuals through the exclusion of independent contractors from employment law protections has, however, led to some legislated intervention in the form of statutory presumptions that operate to re-characterise independent contractors as employees when certain factors are present.

This chapter aims to provide some insight into how South African law has sought to meet the challenges of distinguishing independent contractors from employees and to regulate the issue in a way that minimises the scope for abuse while allowing space for genuine independent contracting.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

The main pieces of employment legislation, chief among which are the Labour Relations Act 66 of 1995 (“LRA”) the Basic Conditions of Employment Act 75 of 1997 (“BCEA”) and the Employment Equity Act 55 of 1998 (“EEA”), apply to employees and not independent contractors. The term “employee” is defined to mean any person, excluding an independent contractor, who works for another person or for the State and who receives, or is entitled to receive, any remuneration, and any other person who in any manner assists in carrying or conducting the business of an employer.

Independent contractors are thus specifically excluded from the application of the employment legislation in question. However, there is no statutory definition of the term ‘independent contractor’. As a result a number of tests have been established through a combination of case law, the introduction of a presumption of employment provision in the LRA and BCEA in 2002, and a Code of Good Practice on “Who is an Employee” issued under the LRA in 2006.

a. Factors that Determine Who is an Employee and who is an Independent Contractor

South Africa’s common law recognised the distinction between a contract of service (an employer-employee relationship under which the employee subordinated his or her services to the authority of the employer - a *locatio conductio operarum*) and a contract for services (a principal – independent contractor relationship where the former contracts the latter to deliver certain services and there is no subordination by the contractor, who instead is answerable to the service deliverables contracted for – a *locatio conductio operis*). Importantly, however, South African courts will not be bound by the labels that parties chose to attach to their relationship or defer to the declared intent of the parties in this regard, whether in their contract or elsewhere. Thus, stipulating

in a contract (or elsewhere) that a relationship is one between independent contractor and principal or referring to the contract as an independent contractor or consultancy agreement, when the relationship between the principal and the contractor is, in reality, one between employee and employer, does not make the relationship any less of an employment relationship, and vice versa.

Over the years the courts have evolved various tests for distinguishing an employment relationship from an independent contractor relationship.

They have identified a number of primary characteristics of employment contracts and independent contractor contracts that may assist in distinguishing the nature of the relationship. These primary characteristics can be summarised as follows:

EMPLOYMENT CONTRACT	INDEPENDENT CONTRACT
the object of an employment contract (or 'service contract') is the rendering of personal services by the employee	the object of a contract with an independent contractor (or 'contract of work') is the production of a specified result
the employee must usually perform the services personally	an independent contractor may usually also perform through others
the employer may choose when to make use of the employee's services (subject to its duty to compensate the employee)	the time for performance by the independent contractor is usually specified
the employee usually performs his or her services under the supervision and control of the employer	the independent contractor works subject only to the contract
an employment contract is terminated by the death of the employee	the death of an independent contractor does not necessarily terminate a contract of work
an employment contract terminates on expiration of the period of service contracted	a contract of work usually terminates on completion of the specified work or production of the specified result

The prevailing approach of the courts is one that can be described as a "reality approach", which involves assessing the reality of the relationship by taking account all of the relevant factors on a substance-over-form basis, the public interest and the fact that parties have no licence to artificially take themselves out of the scope of important legislation such as the LRA, the BCEA and the EEA. The objective is to ascertain the true relationship between the parties. When considering the factors relevant to this question, no single indicator is regarded as decisive (although some are more influential than others) and an examination of the relationship between the principal and the contractor as a whole is required in order to arrive at a conclusion as to whether the relationship is one of employment or not. However, the most recent authoritative judgment¹ on the issue of determining whether an employment relationship exists for employment law purposes has highlighted that the three most important factors are:

i. Whether the principal has rights of **supervision and control** over the contractor, i.e. whether the contractor is obliged to follow the instructions of the principal, including whether the principal is able to dictate to the contractor when he/she is required to

render their services, the manner in which such services are rendered and generally whether the contractor is at the principal's 'beck and call';

ii. Whether the contractor forms **an integral part of the principal's organisation**, e.g. whether the contractor participates or is an integral part of the principal's internal management and/or staff structures; whether the contractor is 'part and parcel of the organisation' or whether the work done is for the business but is not integrated into it and is only accessory to it; whether the contractor would appear to an outsider to be an employee of the principal (e.g. is the contractor provided with a company email address, contact telephone number, business card, dedicated office space at the principal's premises, and is the contractor able to hold him/herself out to others as an employee of the principal). The above said, the fact that a contractor may be required to carry an identity card, wear a uniform and use branding associating them with the principal does not necessarily make him or her an employee – in owner-driver cases, for instance, contractors that had to carry such identity cards, wear such uniforms and use the principal's branding on their vehicles (and even where the purchase of the vehicles was financially assisted by the principal) were nevertheless found to be employees taking into account the other circumstances of the relationship²;

iii. Whether the contractor is **economically dependent** on the principal or whether he/she is free to derive income from other sources as well. The courts have differentiated between personal dependence and economic dependence in this regard. A person who is truly self-employed cannot be economically dependent on their "employer" when he or she retains his or her ability and power to contract with and render services to other persons or entities. This means that an individual who is still free to provide his services to other persons will likely not be regarded as an employee on account of retaining this freedom to contract with and render services to others. Whether or not the individual actually exercises this freedom is strictly speaking irrelevant for determining if the relationship is an employment relationship or not, but if he/she has done so and thereby renders services to a multiplicity of different persons, he/she is more likely to be regarded as an independent contractor.

The above three factors are not the only factors to be taken into consideration; instead, the relationship as a whole needs to be examined in conjunction with the various considerations above, in order to draw a conclusion as to the true nature of the relationship between the company and the contractor. All relevant factors that emerge from an examination of the realities of the parties' relationship must be considered.

The above factors, along with others, have also been incorporated in a rebuttable presumption introduced in the LRA and the BCEA in 2002, specifying when certain lower-earning individuals will be presumed to be employees.

The statutory presumption as to who is an employee

Under the LRA and BCEA, a person who earns less than an earnings threshold amount determined by the Minister of Labour in terms of the BCEA³, and who works for or renders services to another person, will be presumed – until the contrary is proved and regardless of the form of the contract – to be an employee of the other person if one or more of the following factors are present:

- the manner in which the person works is subject to the control or direction of the other person;
- the person's hours of work are subject to the control and direction of the other person;

² Phaka & 19 others v Commissioner Bracks & others (JA 3/2014) [2014] ZALAC 73

³ R205,433.30 per annum as at the end of 2016

¹ State Information Technology Agency (SITA) (Pty) Ltd v CCMA & others [2008] 7 BLLR 611 (LAC)

- in the case of a person who works for an organisation, the person is a part of that organisation;
- the person has worked for the other person for an average of at least 40 hours per month over the last 3 months;
- the person is economically dependent on the other person;
- the person is provided with tools of trade or work equipment by the other person; or
- the person only works for or renders services to the other person.

Other indicators

Some of the other circumstances commonly considered when assessing the nature of a relationship include the following:

Payment / remuneration arrangements. Where payment or remuneration is paid on a regular, periodic basis (e.g. monthly) based on hours worked, this will indicate employment. Independent contractors, on the other hand, are usually paid specified amounts for reaching pre-agreed deliverables upon submission of an invoice after the achievement of the deliverable;

Provision of tools of the trade or equipment. Where the person has to provide their own tools of the trade and equipment, this will indicate an independent contractor relationship. An independent contractor is likely to invest in his or her own assets and use their own tools and equipment of trade, whereas an employee is more likely to use tools and equipment provided by his or her employer;

Expenses. An employee will usually be reimbursed by his or her employer for expenses incurred in the performance of his or her work, while an independent contractor will typically bear his or her own business expenses; and

Benefits. Benefits such as paid leave, allowances and contributions to benefit funds are typical of an employment relationship. Where an independent contractor receives such benefits from his or her principal, this will tend to indicate that the relationship is really one of employment.

Does the fact that the contractor is an incorporated entity make a difference?

While it is so that, where the contractor is an incorporated entity, this will tend to indicate an independent contractor relationship (because employers do not typically engage companies as employees), the courts have not hesitated to find that an employment relationship exists where the substance of the relationship is really between the principal and the individual representing the incorporated entity, and the individual is working as if he/she is an employee of the principal.⁴

b. General Differences in Tax Treatment

The correct classification of a relationship as either employment or independent contracting is also important as a result of the differences in tax treatment. In terms of the Fourth Schedule to the Income Tax Act employers (as defined) who are South African residents and who pay (or are liable to pay) remuneration (as defined) to any employee (as defined) have a duty to deduct or withhold employee's tax from an amount of remuneration before paying it to the employee. The amount of an employee's tax withheld must be paid over to the South African Revenue Services ("SARS").

Aside from certain exceptions, independent contractors do not earn "remuneration" as defined, and the withholding obligation of the Fourth Schedule will not apply.

The Income Tax Act provides for its own statutory tests for determining whether a person is an independent contractor or an employee earning remuneration:

i. The exclusion from the definition of "remuneration" in the Fourth Schedule to the Income Tax Act provides two statutory tests, which deems a person not to be an independent contractor for employees' tax purposes. The statutory tests provide for a deeming provision that a person shall not carry on a trade independently if the services or duties are required to be performed mainly at the premises of the client **and**:

- the worker is subject to the **control** of any other person as to the manner in which his duties are or will be performed, or as to the **hours** of work; or
- the worker is subject to the supervision of any other person as to:
 - the manner in which his duties are or will be performed; or
 - the hours of work.

ii. Where any one of the above statutory tests apply positively, the worker will be deemed not to be an independent contractor and the amount paid to the worker will therefore be included in remuneration and the principal will have to withhold income tax.

iii. Despite the above, a person who employs three or more full-time employees, who are not connected persons in relation to such person and are engaged in that person's business throughout the particular year of assessment, will be deemed to be carrying on a trade independently.

iv. Control of manner

In terms of a SARS Interpretation Note (Note 17), the employer controls the manner in which work is done either by detailed instructions, by training, by requesting that prior approval be sought, or by instituting disciplinary steps in the event of unacceptable performance by the worker, etc. In this regard, "control of manner" means control as to which tools or equipment to use, which other workers to involve or employ, which raw materials to use and where to obtain them, which routines, patents or technologies to use, etc. All of these are elements of commanding and directing an operation to render a particular business result.

SARS Interpretation Note 17 further provides that where the employer has the contractual power to control the manner of use of a worker's productive capacity, it is likely that the employer intended to acquire (and the worker acquiesced to the surrender of) productive capacity. However, the absence of this form of control does not mean that there can be no employee relationship. Any form of control must flow from the legal relationship (the contract) itself and not from some extraneous source (for example, the nature of the trade or profession, the workplace, or market conditions). It is sufficient if the right of control is contractually present, even if it is not exercised in practice.

v. Supervision

SARS Interpretation Note 17 provides that an employer controls the work done and the environment in which the work is done by giving instructions as to the location, when to begin or stop, pace, order or sequence of work etc. It should be noted that, the greater the degree of supervision (that is, the scope or extent of instructions, or the sanctions for non-compliance), the greater the indication in favour of employee status. Any form of supervision must flow from the legal relationship (the contract) itself and not from some extraneous source like the nature of the trade, profession, workplace or market conditions. It is sufficient for the right of control to be contractually present, even if it is not exercised in practice.

Furthermore, SARS Interpretation Note 17 provides that a restraint of trade involves control of the future use of productive capacity, and is intended to prevent unfair com-

⁴ State Information Technology Agency (SITA) (Pty) Ltd v CCMA & others [2008] 7 BLLR 611 (LAC)

petition by protecting sensitive business information, as well as to promote stability of employment. Although a restraint of trade can be imposed on an employee or an independent contractor, independent contractors would ordinarily be subject to a “secrecy clause”. A restraint of trade would tend to indicate an employment relationship.

However, even if the relevant contractor qualifies as an independent contractor in terms of the Income Tax Act tests above, SARS is of the view that consideration must then also be had to a common law test, namely a so-called ‘dominant impression’ test. SARS has developed a guideline in the form of a common law dominant impression grid, aimed at providing guidance as to whether or not there is a dominant impression that the relevant individual is an independent contractor or an employee. The grid sets out the more common indicators in tabular form but is not meant to be exhaustive. The indicators provide insight into the quality of control, the nature of financial relations and the degree of exclusivity of the relationship. The indicators have been classified into three categories, namely:

- near-conclusive (those relating “most directly to the acquisition of productive capacity”);
- persuasive (those establishing “the degree of control of the work environment”); and
- resonant of either an employee/employer relationship or an independent contractor/client relationship, whichever is relevant.

Each indicator in the grid must in itself be analysed with due regard for the particular context (kind of industry, kind of business, kind of customer, kind of worker), and how the business actually operates. One must analyse the relationship in light of all the indicators and their relative weightings, and arrive at a dominant impression in favour of either the acquisition by the employer of the worker’s productive capacity (that is, of labour power, capacity to work, or simply effort), or of the result of the worker’s productive capacity. This dominant impression will be the basis for classification of the relationship as either an employee relationship or an independent contractor relationship.

Expatriates

Expatriate employees performing services in South Africa may in certain instances be required to pay South African employee’s tax on South African sourced income, subject to any double tax arrangements which may be in place between South Africa and the expatriate employee’s home country. This aspect will require careful consideration of the factual circumstances on a case by case basis.

In terms of the definition of “remuneration” contained in paragraph 1 of the Fourth Schedule to the Income Tax Act, a person who is not a resident cannot qualify as an independent contractor. Expatriate independent contractors working in South Africa will therefore be subject to a tax withholding obligation on any South African sourced income.

Registration for Value-Added Tax

Independent contractors who carry on an “enterprise” as defined in the Value Added Tax Act 89 of 1991 (“VAT Act”) may be obliged to register for VAT purposes in South Africa. The obligation to register for VAT will generally arise if the ‘enterprise’ has taxable income (comprising of standard rated and zero rated supplies) with a value of more than R1 Million per annum.

c. Differences in Benefit Entitlement

Employees in South Africa are entitled to certain minimum employment benefits, while independent contractors are not.

Employees

Subject to some exclusions, all employees are entitled to a number of statutory minimum entitlements and basic conditions of employment.

Basic conditions

The BCEA sets general mandatory rules relating to basic conditions including the regulation of working time, leave, particulars of employment and remuneration (although there is currently no prescribed national minimum wage), termination of employment and the prohibition on the employment of children and forced labour. For certain sectors (such as for example farming, hospitality, domestic workers etc.) there are also sectoral determinations published by the Department of Labour providing for certain conditions of employment applying only to that sector which may be different from the conditions as per the BCEA, including but not limited to minimum wages particular to those sectors.

The BCEA statutory minimum employee benefits and conditions of employment are briefly as follows:

- employees may not be required to work more than 45 ordinary hours in any week and 9 ordinary hours on any day (if the employee works 5 days a week) or 8 hours on any day (if the employee works more than 5 days a week);
- employees may not be required to work more than 10 hours overtime in any week, and any overtime hours worked will generally attract enhanced pay;⁵
- employees who work continuously for more than 5 hours are entitled to a meal interval of 1 continuous hour, but agreement may be reached to reduce the meal interval to 30 minutes or to dispense with a meal interval for employees who work less than 6 hours a day;⁶
- employees are entitled to a daily rest period of at least 12 consecutive hours and a weekly rest period of at least 36 consecutive hours which should include a Sunday (unless agreed otherwise);⁷
- work on Sundays is permitted but such work will attract enhanced rates of pay;⁸
- work on public holidays is permitted provided that the employee has agreed to do so, and any such work will attract enhanced rates of pay;⁹
- night work is regulated and may attract additional payments such as night work allowances;¹⁰
- employees are entitled to 21 consecutive days annual leave (i.e. 15 working days, if the employee works 5 days a week) per annual leave cycle of the 12 months¹¹, sick leave equivalent to the number of days worked during a 6 week period for every 36 consecutive months¹², 3 days family responsibility leave per year and qualifying employees are entitled to 4 consecutive months’ unpaid maternity leave;¹³ and
- employees are entitled to minimum periods of notice of termination.¹⁴

Statutory regulation of working hours, overtime work, night work and work on Sundays and public holidays does not apply to senior managerial employees, sale staff who travel and regulate their own working hours, employees who work less than 24 hours a month and employees who earn more than the BCEA earnings threshold¹⁵.

⁵ Section 11(2)(b) of the BCEA

⁶ Section 14 of the BCEA

⁷ Section 15 of the BCEA

⁸ Section 16 of the BCEA

⁹ Section 18 of the BCEA

¹⁰ Section 17 of the BCEA

¹¹ Section 25 of the BCEA

¹² Section 20 of the BCEA

¹³ Section 22 of the BCEA

¹⁴ Section 37 of the BCEA

¹⁵ Section 6 of the BCEA. See above for the BCEA earnings threshold.

Compensation funds

Employees are also entitled to claim compensation benefits for work-related injuries and diseases¹⁶ and unemployment and maternity pay¹⁷ from statutory compensation funds, to which employers contribute.

Unfair labour practice protection

Employees may not be subjected to unfair labour practices.

Health and safety

Under the Occupational Health and Safety Act [] of 1993, employers owe all their employees statutory duties to maintain a safe workplace and minimize the exposure of employees to workplace hazards.

Independent contractors

As opposed to employees, independent contractors are only entitled to such “benefits” and terms as have been agreed to between the independent contractor and his / her client.

Independent contractors are not entitled to any of the statutory minimum employment-related entitlements highlighted above, save that, in the case of health and safety, while they do not qualify as ‘employees’ under the Occupational Health and Safety Act, the principal still owes them the general duties that are owed to persons other than employees under the Act, namely the principal must conduct its business in such a manner as to ensure as far as is reasonably practicable that persons other than its employees who may be directly affected by the principal’s activities are not thereby exposed to hazards to their health or safety.

d. Differences in Protection from Termination

Employees are protected against the unfair termination of their employment by an employer. The LRA requires any termination of employment to be substantively fair (i.e. for a fair reason) and procedurally fair (i.e. after following a fair procedure). Accepted fair reasons for dismissal are misconduct, incapacity (ill-health and work performance) and operational requirements of the employer (i.e. redundancy or restructuring).

The BCEA also provides for certain minimum notice periods that must be adhered to when terminating on notice, with the minimum periods ranging from 1 weeks’ notice during the first 6 months of employment to 4 weeks’ notice if employed for more than a year (or if the employee is a farm worker or domestic worker who has been employed for more than 6 months)¹⁸. Employees may not be required to give longer notice of termination than the employer but an employer may elect to pay an employee in lieu of notice¹⁹.

Upon termination of employment employees are also entitled to certain statutory minimum termination pay-outs such as pay in lieu of notice (if the employee is not required to work out his notice period), payment for any accrued but untaken annual

leave and payment of any other accrued amounts which remain unpaid. If the reason for termination relates to the employer’s operational requirements the employee will also be entitled to severance pay equal to no less than 1 weeks’ remuneration for every completed year of service.

Independent contractors, on the other hand, do not enjoy any protection from the

¹⁶ Compensation for Occupational Injuries and Diseases Act [] of 1993

¹⁷ Unemployment Insurance Act [] of 2001

¹⁸ Section 37 (1) of the BCEA

¹⁹ Section 38 of the BCEA

termination of their contracts other than general protections against contractual breach and common law unlawful termination. Termination of independent contracting relationships is therefore governed by the agreement between the parties.

e. Local Limitations on Use of Independent Contractors

There are no specific local limitations on the use of independent contractors.

f. Other Ramifications of Classification

Discrimination

While contractors do not enjoy protection against unfair discrimination under the Employment Equity Act, as this Act only applies to employees or applicants for employment, they enjoy similar protection under the Promotion of Equality and Prevention of Unfair Discrimination Act [] of [].

Vicarious liability

An employer is vicariously liable for its employees’ actions performed during the course and scope of their employment, but a principal it is not liable for any actions committed by an independent contractor in the course and scope of the contractor’s work for the principal.

Obligation for a foreign company to register in South Africa as an external company

For foreign companies the correct classification of an individual as an employee or independent contractor can also be important for purposes of compliance with South African company laws. Foreign companies who have no presence in South Africa but who are party to an employment contract within South Africa are required to register as an external company with the Companies and Intellectual Property Commission in South Africa within 20 days of entering into the employment relationship. The compliance consequences of such a registration are mostly administrative in nature, but there is an obligation to continuously maintain at least one office in South Africa.

g. Leased or Seconded Employees

Temporary employment services

Atypical employment relationships such as the use of leased workers from temporary employment services (commonly referred to as labour brokers in South Africa) are expressly regulated in South African employment legislation (primarily the LRA). A labour broker is defined as a person who, for reward, procures for or provides to a client other persons who perform work for the client and who are remunerated by the labour broker. Where a labour broker supplies employees to a client under a labour broking arrangement that complies with the legislation, the labour broker is regarded as the employer of the labour broker employees to the exclusion of the client. Notwithstanding this, the client will be jointly and severally liable with the labour broker if the labour broker (in respect of its employees supplied to the client) contravenes a collective agreement concluded in a bargaining council regulating terms and conditions of employment, a binding arbitration award that regulates terms and conditions of employment, the BCEA or a sectoral determination.

In addition to the above, labour broker employees who earn less than the BCEA earnings threshold are entitled to additional protections in terms of section 198A of the LRA. An employer (i.e. the client) who uses such labour broker workers for longer than 3 months is deemed to be the employer of the labour broker employees and, unless the labour broker employee is employed on a fixed term basis in accordance with section 198B of the LRA, the labour broker employee will be deemed to be indefinitely employed by the client.

The legal and practical consequences of this deeming provision have not yet been finally determined but at the very least it will result in:

- the labour broker employees having to be treated on the whole not less favourably than the employees of the client who perform the same or similar work than the labour broker employees, unless there is a justifiable reason for the difference in treatment;
- the client and labour broker will be jointly and severally liable for the contravention of a collective agreement concluded in a bargaining council regulating terms and conditions of employment, a binding arbitration award regulating terms and conditions of employment, the BCEA or a sectoral determination;
- the labour broker employees may institute proceedings in terms of the LRA (including but not limited to unfair dismissal and unfair labour practice claims) against either the client or the labour broker, and any award or order in this regard against either, may be enforced against either the client or the labour broker.

Secondment of employees

Secondment of employees is an accepted practice in South Africa, and may take place on account of an agreement between the employee, his employer and the entity to which he will be seconded. Depending on the specific circumstances of the secondment, it may result in the employee qualifying as an employee of both employers involved in the secondment.

h. Regulations of the Different Categories of Contracts

South African employment law is protective of employees and many aspects of the employer/employee relationship are regulated by legislation and, in highly unionised industries, by collective agreements. As indicated above, the BCEA regulates basic conditions of employment and impacts directly on what can be provided for in employment contracts (in industries where a sectoral determination has been issued or there is a bargaining council under which industry collective agreements are concluded, these instruments will further regulate what may be provided for in employment contracts in those industries). The LRA also provides substantive regulation for the termination of the employment relationship and employment contracts, whether the employment contract is for an indefinite or a definite period, as well as unfair labour practice protections for employees.

There is no specific national legislation regulating independent contractors or a self-employment relationship. The general civil, commercial and corporate laws will apply.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

The re-characterization of an independent contractor as an employee can only take place by a Court or arbitration award, and will only occur where the reality of the nature of the relationship is found to be one of employment, despite the fact that the parties may have labelled their relationship as one of principal / independent contractor. Re-characterization usually takes place where the contract with the independent contractor is terminated by the principal and the contractor wishes to reinstate the contract or obtain termination benefits, and seeks to do this by claiming that he/she is in fact an employee before employment tribunals or courts.

b. The Legal Consequences of a Re-Characterisation

A failure to correctly characterise a relationship as an employment relationship exposes the employer to a number of legal risks when it is re-characterized:

i. Where the contract has been terminated by the employer, the employer will be exposed to unfair dismissal remedies. The primary remedy is reinstatement (even for senior employees) or re-employment, with or without back pay. Absent reinstatement or re-employment, financial compensation of up to 12 months remuneration could be awarded.

ii. If the contractor, re-classified as an employee, earns at a level that qualifies him / her under the BCEA for overtime pay, the employer could be liable for historic overtime pay. Moreover, in terms of the BCEA, a failure by an employer to comply with any provision of the BCEA or to pay any amount due in terms of the BCEA, may expose the employer to the risk of liability for the payment of a fine. For contraventions not involving the underpayment of any amount, fines ranging from R300 to R1500 per employee in respect of whom the failure to comply occurs, may be ordered. For contraventions involving underpayments, the fines range from 25% to 200% of the amount due, including any interest owing on the amount at the date of the order.

iii. The employer could be liable for historic unpaid annual leave owing to the contractor qua employee.

iv. If the employer has not been withholding income tax, it could be required by SARS to pay the income tax (and possibly fines) and would then be left with the challenge of recovering this from the contractor. The above said, there may also be further adverse tax consequences for the contractor as SARS may re-examine his / her tax returns for the duration of the contract and disallow deductions sought and obtained by the employee on the basis that he/she was an independent contractor.

v. If the employer has not been making social security contributions (unemployment insurance contributions, skills development levies, etc.) it could be required by the authorities to make good these payments.

vi. Although South Africa does not have any compulsory national retirement or superannuation contribution framework, if the employer has an occupational, company-specific retirement scheme it will often be the case that the scheme rules require compulsory membership and contributions for all employees of the employer and this could result in the employer being liable to make good contributions that should have been made (although this is rare in practice).

vii. As indicated earlier, where the employer is a foreign company that is not already registered in South Africa as an external company, re-characterisation of a relationship to one of employment may also trigger an obligation to register as an external company in terms of the Companies Act.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

An individual whose services have been engaged on an independent contracting basis, but who seeks employee status usually tries to assert his / her claim for employee status when the principal terminates the contract. The individual will then typically refer a dispute to an employment tribunal (usually the Commission for Conciliation, Mediation and Arbitration²⁰) or the Labour Court, claiming that he/she is an employee and that

²⁰ A statutory body tasked with resolving employment disputes either by way of conciliation (negotiation with the aim of settlement) or arbitration.

he/she has been unfairly dismissed. The principal has the opportunity to dispute the individual's claim before the tribunal / Labour Court.

Should the individual be successful in proving that the relationship is in reality one of employment and that the dismissal was consequently unfair, as indicated above the individual could either be reinstated or re-employed (i.e. as an employee), or could be awarded compensation of up to 12 months remuneration for unfair dismissal. The payment of other basic conditions of employment could also be ordered. As regards tax, the Labour Court has in the past directed that a copy of the judgment (determining the employee status of the individual) be sent to SARS so that SARS can deal with the tax consequences.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

A written contract should be concluded. The terms of the contract should reflect the characteristics of an independent contractor relationship as identified above, for example it should, if possible, state that:

- the contractor is an independent contractor and not an employee and that the parties do not intend their relationship to be one of employment;
- the contractor is free to control and organize his / her own manner of working and his / her working time;
- payment is based on specified deliverables/results being achieved;
- the contractor is free to contract with and do work for other companies, etc.
- it should avoid terms generally associated with an employment contract and relationship, such as any provisions relating to employment-type benefits, references to 'employment', salary, wages, leave, etc; and
- the nature of the services, the apportionment of risk, remedies in the event of breach and liability for tax should be clearly and expressly provided for.

b. Day-to-Day Management of the Relationship

In light of the fact that the true nature of the relationship is determined with reference to the day to day reality of the relationship, not just the terms of the contract, it is important for the principal to ensure that the independent contractor is not in reality treated as an employee. The management of the day-to-day relationship must be consistent with the contractual arrangements. Practically, therefore, the level of control exercised over the independent contractor should be limited and care should be taken not to unduly limit the independent contractor's ability to contract with other entities. The principal should give the contractor as much independence as possible.

V. TRENDS AND SPECIFIC CASES

Whilst the exercise to determine if an employment relationship exists is dependent on the factual circumstances of each case, recent case law suggests that the legal tests to make this determination are now widely accepted. Recent case law has accordingly

confirmed the legal tests as previously set out by our courts and it is not expected that the test(s) as set out above will be greatly changed in the near future. Authoritative cases include:

- *State Information Technology Agency (SITA) (Pty) Ltd v CCMA & others* (supra), in

relation to the general tests and key factors in the determination of the true nature of the relationship;

- *Phaka & 19 others v Commissioner Bracks & others* (supra) in relation to owner-driver schemes and the nature of such relationships; and
- *Denel (Pty) Ltd v Gerber* in relation to assessing the effect of the use of an incorporated entity by an independent contractor.

Whether or not Uber's relationship with its drivers is in the nature of an independent contractor or employment relationship is currently pending before South Africa's main employment tribunal.

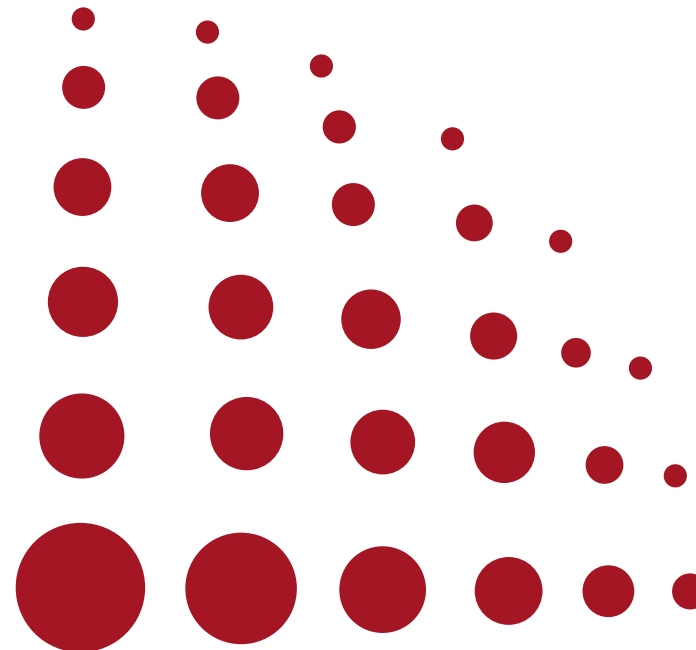
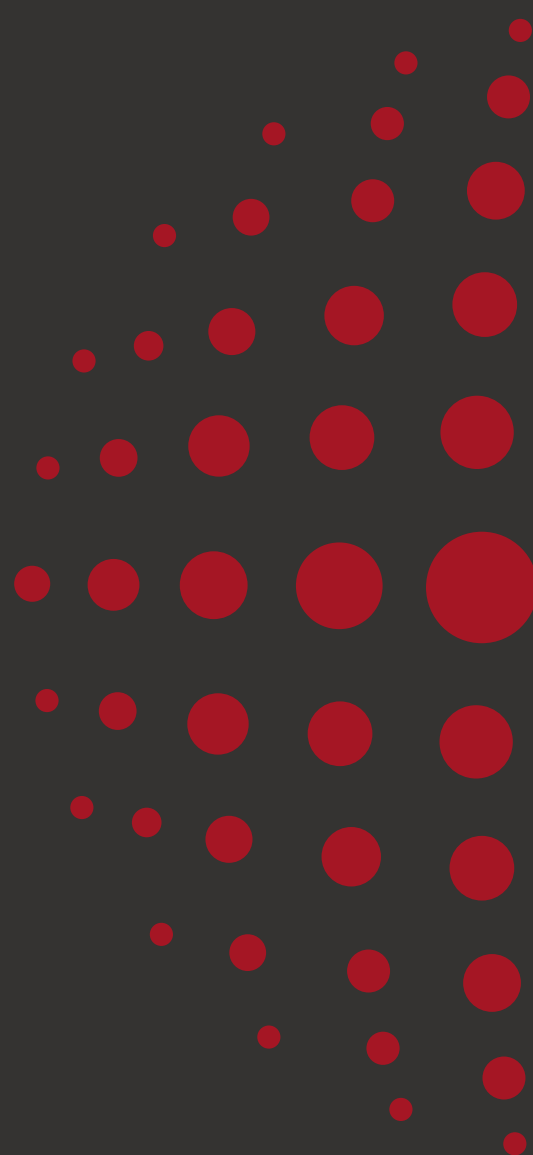
In 2016 the trade union movement and other activists continued their campaign against the use of labour brokers and outsourced managed services providers (i.e. independent contractors), with this issue being one of those in the spotlight during a wave of university student protests regarding high university fees and demands for an end to outsourcing of non-core services at universities. It seems likely that this demand will spill over into 2017 and perhaps into other industries.

VI. CONCLUSION

In South Africa, while the concept of an independent contractor, as distinct from an employee, has long been recognised and the tests for determining this have been refined by the courts over the years, the line between who is an employee and who is an independent contractor is often blurred by the factual peculiarities and idiosyncrasies of the particular relationship, especially with modern ways of work and the use of technology challenging traditional notions of how an employment relationship operates. Incorrectly classifying the relationship can have significant implications for the employer, with the result that employers would be well-advised to give proper consideration to the nature of the relationship when entering into it, to ensure that they correctly characterise it in a clear written contract agreement and to monitor that the practical reality of the day-to-day management of the relationship is consistent with the contract, because South African tribunals and courts will examine the reality of the nature of the relationship when determining its classification.

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SPAIN

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I. OVERVIEW

a. Introduction

The present article will analyze the differences between an employee who has an employment relationship with its employer and an Independent Contractor who has a mercantile relationship of independence with the Company (its client).

In this sense, it will hereby be explained what is required for the existence of an employment relationship, concluding that it is especially necessary that the Company (receiver of the services) assumes the costs, risks and economic results inherent to the productive activity (what is known as “alienation”), as well as a degree of dependence or subordination of the employee with regards to the employer, being included in its governing, disciplinary and organizational circle.

Thus, we will see how the independent contractor does not comply with the characteristics mentioned above, since it will be in charge of organizing its own work, making use of its own resources and assuming the risks of its activity.

Another difference between an employee and an independent contractor is the type of contract that regulates the employment relationship, which may be set for an indefinite or temporary duration. On the other hand, the contract that regulates the specificities of an independent contractor may be civil or commercial. However, it should be taken into account that despite of the type of contract that the company uses, in the event of a conflict, the principle of primacy of reality will always be applied in order to decide whether the person is an employee or an independent contractor.

If a person claims for the recognition of the labor nature of its relationship with the employer, two assumptions may arise with their respective consequences, depending on whether (i) the employee can demonstrate the existence of an employment relationship while continuing providing services, or (ii) the employee interposed the claim after being dismissed and got a favorable judgment. In both cases, if the plaintiff obtains a favorable and final decision, the following step would be to report the current situation to the Labor Inspectorate. The public authority would then request the Company for the unpaid Social Security contributions accrued during the last 4 years prior to the filing of the claim.

In the present article, we will also make a comparison of the Tax aspects between independent contractors and employees, such as the income tax (IRPF), VAT and social security contributions.

Another topic that we will be discussed in this work will be the main differences between the General Social Security and the Special Social Security Scheme for independent contractors, which may have different effects on retirement, maternity and paternity benefits.

Due to its importance, we will also explain the figure of the independent contractor economically dependent (hereinafter “TRADE”), who constitutes a special category of independent contractor that mainly work for one client.

Finally, we will discuss the same case seen from two different perspectives in order to be able to distinguish the difference between an employee and an independent contractor.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine the existence of an Employee or an Independent Contractor

The legislator does not provide a clear definition on the concept of “*contract of employment*”, but we can figure it out by looking at the Workers’ Statute (*Estatuto de los Trabajadores*) and its delimitation of the scope: it refers to workers who provide their services voluntarily, paid by others, and within the organization and direction of another person or legal entity, called employer or businessman.

Then, characteristic features of wage labor can be found, and so forth, on the contract of employment, as a link that regularizes the provision of such services, and for which a person (the employee) agrees to carry out an activity, for some time (definite or indefinite), in the context of organization under the direction of another (the employer) in return for payment.

However, for a relationship to be born, a real service taking place or a precise activity made personally and voluntarily, whether paid or unpaid, is insufficient; we need to join those other elements, which are precisely the provisions allowing us to qualify it as “work”, particularly the assumption of the costs, risks and individual economic results of productive activity by the service receiver (alienation), as well as dependence or subordination of the worker on the employer, being within its disciplinary and organizational circle.

The employment relationship has a “statutory assumption” status in Spain as the Workers’ Statute establishes that there is an employment relationship every time work is performed under someone else’s direction, organization and account, for remuneration.

Regarding the definition of independent contractor, in the legislative landscape there are several definitions of self-employed, both in the area of Social Security as well as in others (e.g. in the construction sector). For reasons of legislative modernity and coherence, the reference should be to that established by the Law 20/2007 of July 11, approving the Statute of Independent Contractors.

Independent contractors are natural persons who carry out, on a regular basis, personally, directly, on their own account and outside the sphere of management and organization of another person, an economic or professional activity for profit, whether or not being employed.

The following are automatically included under the scope of application of the Statute of Autonomous Work, provided that they comply with the requirements indicated above (and without prejudice to the provisions of their respective specific rules):

- the industrial partners of joint-stock companies and limited partnerships.
- community members of communities of goods and members of irregular civil societies, unless their activity is limited to the mere administration of the goods in common.
- those who exercise the functions of management and management that involves the performance of the position of director or administrator, or provide other services for a capitalist company, on a profit and in a regular, personal and direct manner, when they have the effective, direct or indirect control.
- economically dependent self-employed workers.
- foreign self-employed workers who meet the requirements set out in the regulations on immigration law.

It is important to know that the qualification of the contract does not depend on how it was determined by the parties but by the effective configuration expressed in the obligations accepted under the agreement and its performance - “primacy of facts” principle.¹

To this extent, the factors that will determine the distinction between an employee and an independent contractor are the following:

- dependence
- alienation
- personal nature of the relationship
- payment
- exclusivity and assiduity

Dependence

The employment nature of the bond is not denied by the breadth of the degree of autonomy available to the worker when performing the service, but to consider a services relationship as “work”, it must happen within the scope of organization and direction of the employer, jointly providing personal services, and the consequent alienation to the company’s risk taking action².

Case law has even held that “dependence” is the most decisive vertebral element in the employment relationship.³

However, this element cannot be understood as a strict subordination of the employee to the employer, so in order to appreciate it, it is enough for the worker to be within the rector and disciplinary circle of the company.⁴ It involves conducting professional activity within the organization and direction of the employer, so that the employer can permanently modulate the content of the delivery required for the worker.

In contrast, there is no labor relation when a person has his own business and acts as a labor entrepreneur.⁵

The Courts nowadays are declaring that there are common signs of dependence: the assistance at work or a place designated by the employer and the submission to a timetable, the personal performance of work, supported in certain services with an exceptional regime of substitutions or replacements, the participation of workers in the employer’s workplace organization, which is responsible for scheduling his activity and, on the contrary, the absence of the worker’s own business organization.

Alienation

This concept is useful to explain that the employee is rendering his services to another, which is called the employer.

They hold different criteria to apply it:

- Alienation because of the fruits.
 - It reveals that the essential and defining facts on an employment contract lay on his fruits, fruits that, from the first moment of production will belong to someone else, but never to the worker.

¹ (STS 11 December 1989, STS 29 December 1999, among many).

² Supreme Court 20/09/84; TS 11/10/83.

³ Supreme Court 05/14/90).

⁴ Supreme Court 10/22/83; 11/11/83; 23/09/85.

⁵ Supreme Court 4.7.87.

- Alienation because of the risk. From this perspective, three essential characteristics are required:
 - Labor costs to be assumed by the employer;
 - The fruit or result of the work to be incorporated into the assets of the employer;
 - Economic results depending on the employer, but the worker is not affected by it, nor is his participation in the economic risk.
- Alienation because of the market.
 - The product of the work provided by the employee is not going to the market directly but has to pass through another person: the employer or the business.

Alienation assumes that the worker does not retain ownership of the outcome of his work, which is transmitted to the employer, who incorporates it as its own market. Thus, there will not be a labor relationship if both profits and losses are taken as a risk by the worker.

The company contribution of appliances, instruments and necessary equipment for the development of the work, are a sign of alienation.⁶

A contrario of what was said hereinabove, workers who personally and directly carry out an economic activity for gain is classified as a self-employed worker.

The existence of arrangements for payments under the benefits or outcomes (profit sharing, commissions, performance bonuses) considering that a minimum wage is guaranteed for the worker, is not an obstacle to the consideration of alienation.

Very personal nature

The personal side of the employment relationship is based on two different affirmations: First of all, we have to bear in mind that the employee can only be a natural person – and not a legal person. Then, this employee cannot be exchanged. The employment contract is an *intuitu personae* relationship. The employer hired his employee because of his own skills, experience and identity and those elements are essential to the contract.

Payment

In order to appreciate the existence of a labor contract, it is compulsory that the activity is made in an exchange with the compensation coming from the employer, without regard to its precise form (wages, bonuses, etc).

On the contrary, an independent worker will be paid thanks to services or fees paid by his/her clients.

Exclusivity and assiduity

Both notes have been deeply studied and analyzed by case law.

i. Exclusivity is not a required point, unless there is a full-time agreement⁷, or other work involving unfair competition.⁸ Moreover, the exclusivity clause, during a long period of time and designed in strict terms, enforces the labor consideration of services providing dependence on a relationship of subordination between the parties.⁹

ii. The note of assiduity can be considered a clue that guides us to the existence of an

⁶ TSJ Madrid 15/03/02).

⁷ SC 05.13.86, 06.03.86.

⁸ SC 16/12/86.

⁹ TS 19.04.86, 12-9-88; TSJ País Vasco 19/11/91.

employment relationship.

As part of an antithetical concept of assiduity, briefness of service is another factor, which may exclude the qualification of a relationship as a labor one.

Thus, we can see that the independent contractor does not comply with the feature notes described above, as there is no dependence, because he confronts the whole organization of his own work. In addition, the independent contractor assumes the financial risk of the business (both benefits and losses), not collecting a fixed amount, but one depending on the work performed, and that is the reason why neither alienation and compensation notes can be appreciated here.

b. General Differences in Tax Treatment

In this section, we will make a comparison of tax issues between independent contractor and employees. The taxes that, basically, affect both parts, are Personal Income Tax (IRPF), VAT and social security contributions.

Personal Income Tax

This is a personal, direct and progressive tax that affects incomes earned by individuals in a calendar year. According to that definition, between an independent contractor and an employee, both earning the same income, great differences would not exist when paying this tax, unless, as with the deductible expenses by person, the independent contractor may also deduct that one in addition to its activity.

Both the independent contractor and employee must fill in an annual statement (D -100 model) of personal income tax. Also, the independent contractor will be required to submit quarterly statements of personal income tax installment payments of their incomes (130 or 131 models) as well as the quarterly and annual summaries of withholdings, the incomes practiced in the payroll to their workers and the invoices of professionals (111 model quarterly and 190 model as an annual summary).

Value Added Tax

It is an indirect tax on consumption and falls on the final consumer, so both the independent contractors and employees have to pay VAT on their purchases.

The independent contractor also acts as an intermediary, paying the difference between the VAT that they have passed on to their customers and the VAT that they have incurred on their purchases allocated to the activity, taking into account the quotes of VAT that have affected his bills, regardless of whether he has earned it or not.

Additionally, the independent contractor must submit quarterly VAT self-statements (303 or 310 and 311 models) and also an annual summary (model 390) for informational purposes.

Social Security Contributions

Here is where we can find greater differences between the two figures, both in the determination of the base, as in the types to be applied and for which coverage is protected. Fees for both are calculated in the same way, applying a percentage to a contribution basis.

The base price of the employee, between a minimum and maximum limit depending on the payroll in turn, also depends on the working hours among others. Instead independent contractor choose between a minimum and maximum cap base by going public irrespective of time to devote to the activity and income. Attention must be attracted on the fact that specialties exist in the case of independent contractors who have more

than 47 years and being the baseline in 2016 of 893,10 € per month. The base can be modified twice a year.

The contribution rates vary significantly depending on whether we speak about employees or independent contractors.

For the employees, the rate is 7.05% or 8.30% depending on the type of contract and the employer is required to enter the Social Security Fund fee.

For independent contractors, the total percentage depends on the coverage to which he subscribes, with a minimum of 29.80 % or 26.50% if not quoted by IT (Temporal Incapacity) derived from common contingencies.

A worker compulsorily quotes for common, professional training, Social Guarantee Fund and unemployment.

Independent contractors are required to quote for the coverage of IT for common contingencies, except those that are already covered by another social security scheme (i.e., multiple jobs). The coverage of AT Work Accident) and EP (Professional Disease) is voluntary, except for the TRADE contractors for which it is required. The price for cessation of activity is also voluntary, but if the latter is quoted it is mandatory.

Also at birth and extinction of the obligation to contribute there are differences: as long as a worker quotes by the working period, the independent contractor quotes in full months.

There are other aspects to be taken into account only in the case of independent contractors:

Business Tax

The vast majority of independent contractors are exempt from this tax, a fact, which will be reflected in his statement filled in the Tax Office census prior to the beginning of its activity (036 or 037 model). Otherwise, they must fill in the 840 model.

Annual Statement of operations with third parties

It is a statement (347 model) with character information to be submitted during the month of February, since 2013, indicating those persons or entities, customers or suppliers, with whom the independent contractor has exceeded 3,006 € in the previous year.

c. Differences in Benefit Entitlement

Social Protection programs offered to independent contractors have suffered from significant changes over recent years up to the current configuration of the protective action set to enter into force soon - the Special Scheme for independent contractors.

The protective action of the Special Scheme for independent contractors includes the following features:

- healthcare
- temporary disability
- maternity and paternity
- risk during pregnancy and breastfeeding
- care for children affected by cancer or other serious illness
- permanent disability (total, absolute and severe disability)
- retirement
- death benefits

- professional Contingencies
- provision for cessation of activities
- social care
- social services

We can say that the main differences between the General System of Social Security (GSSS) and the Special Scheme for Independent contractors are in pension benefits as well as maternity and paternity.

As for retirement, its regulation is the same as the GSSS with some specialties:

Age

As of 2016, the normal retirement age is:

- 65, if they quote 36 years or more;
- 65 years and 4 month, if they quote less than 36.

However, in response to the toxic, dangerous or arduous nature of the pursued activities, and in the terms established by regulations, even those which development is still pending, affected independent contractors who meet the conditions to be entitled to order to receive the retirement pension, except for age reasons, can access retirement faster on the same assumptions and collective rights as for employed persons. Also, independent contractors with disabilities will be understood in the same conditions as employed persons.

On the possibility of access to early retirement for a worker who had mutual status to 01.01.1967 and to collect contributions in various regimes and, by applying the rules of reciprocal calculation, the pension should be recognized for according to the rules of the RETA, provided acknowledgment of the age requirement in any of the other schemes that have been considered for the aggregation of insurance periods. Access to early retirement person concerned to the age of 63 years is suspended until 31/03/2013 (RDL 29/2012 disp.adic.1ª).

Amount

In order to calculate the amount of pension applied to the regulatory base, compute the percentage obtained exclusively from the effective contribution years of the beneficiary. The amount to be received as a pension is paid monthly, in two bonuses.

Regulatory base

It is calculated in the same way as with GSSS. If there are gaps, in periods when there was no obligation to contribute, they are not complete as in the GSSS, but these months are overdrawn and yet they are computed as divisor. That is, the corresponding divider remains unchanged despite the months considered as zero-based unlisted.

Origin of the pension

The time of the event originating the pension is:

- for those who are already registered, the last day of the month in which work termination occurs;
- for those who are in a similar service, the last day of the month in which the presentation of the application happens;
- for workers who are not registered, or similar situation, from the application moment.

Leave

The waiting period requires 15 years of contributions, 2 of which must be within the 15

years immediately prior to the contingency. No scale is applied, according to attained age on 01.01.1967, when calculating the contribution years.

As for maternity and paternity leave, independent contractors are entitled to maternity benefits (contributory and non-contributory ones) and also paternity to the same extent and on the same terms and conditions provided for workers in the RGSS, with specialties indicated.

The periods of cessation of activity during which they are entitled to receive the maternity and paternity match, in terms of duration and distribution, the labor rest periods established for employed persons. The only difference is the possibility of receiving the subsidy more compatible with a part-time job, in which case the perception of the subsidy and the reduction of activity can only be made in a percentage equal to 50 %.

If, while collecting the subsidy on a part-time job regime, a process of IT starts, without caring about contingency may, where appropriate, also perceived IT allowance. In this case, the regulatory base of IT allowance is reduced to 50 %.

Thus, the difference with the general scheme is that, by agreement with the employer, resting part-time workers employed by maternity leave, do not set a specific percentage reduction.

d. Differences in Protection from Termination

Upon termination of employment, the employer must provide the employee with:

- company certificate and listing documents useful to the employee, if appropriate, in order to prove and be able to ask for unemployment benefits.
- a document proposing settlement of owed amounts, when communicating the complaint settlement of the agreement or, where applicable, the notice of termination.

It must also make knowledgeable to the company council, documents relating the termination of the employment relationship. A failure to comply with them is punishable as a serious offense in labor with a fine.

As evidence, to prove the termination of the agreement by mutual agreement or will of the worker, the worker may be required to sign the settlement receipt, albeit without it being mandatory.

Indeed, upon termination of the employment contract between an employer and a worker, the first has to pay the employee, in any case, accrued and concepts, such as unpaid wages, the share of bonuses and the amounts of unused vacations. However, independent contractors do not enjoy such protection, as they are individuals who perform on their own and outside the scope of management and organization of another person, a business or professional activities for profit.

Thus, the main difference in the termination of contracts is that in the case of independent contractors, they do not have a liquidation or compensation to attend the no dependency note, however workers under employment relationships do have the right to rely economically on the employer.

However, it should be taken into account that economically dependent worker (TRADE), which are a unique category of independent contractors, to apply it as a general rule, the common system established by the status of self for all the collective independent contractors, subject to certain peculiarities that presents its professional status.

One of those quirks refers to the contract termination and the consequent compensa-

tion, which is regulated by Spanish Law, unlike the independent contractors.

Thus, the contractual relationship between TRADE and his client may be terminated for any reason provided by law, as well as the causes that the parties have agreed to in the contract, unless they constitute abuse of law, and in particular, by any of the following circumstances:

- mutual agreement of the parties.
- death, retirement or disability incompatible with professional activities.
- withdrawal of TRADE, and there must be the advance notice provided or according to custom.
- will the TRADE, found in serious breach of contract by the counterparty.
- will the client for cause, and there must be the advance notice provided or according to custom.
- by decision of the employee who was victim of violence.

In addition, the termination of the contract between the customers TRADE may lead to compensation in any of the following circumstances:

- breach of contract by the other party that sometimes results in damages.
- will the client without cause.
- withdrawal of the TRADE, subject to fulfilling the obligation of notice, when the cause is material injury to halt or disrupt the normal conduct of its business.

e. Local Limitations on Use of Independent Contractors

Those workers who render their services and who do not comply with the requirements deriving from their legal conception are expressly excluded from the scope of the Statute of independent contractors and, in particular:

i. Employment relationships, that is, employed persons.

ii. The activity that is purely and simply limited to the mere performance of the position of director or member of the administrative bodies in companies that have the legal form of a company.

iii. Special labor relations, which are:

- senior executive staff.
- domestic staff.
- convicts who are serving a prison sentence.
- professional sports players.
- artists in public shows.
- individuals intervening in commercial transactions on account of one or more business owners without assuming the risks inherent thereto.
- handicapped workers providing their services at special employment centres.
- port stevedores who provide their services through state companies or individuals who carry out the same tasks as the latter at ports managed by Autonomous Communities.
- any other task that is expressly declared to be a special employment relationship pursuant to the Law.

f. Other Ramifications of Classification

As we know, independent contractors are a group, which operates financially as professional or independent contractors in different economic sectors (agriculture,

fishing, handicrafts, trade, transport, diverse professional, etc.). Within this large group we can distinguish, together with the figure of the classic or ordinary independent contractors, other figures that include the autonomous nature of their business, have their own characteristics, such as economically dependent independent contractors (TRADE). Those particular contractors meet all requirements of any independent contractors themselves and conduct their business primarily for a single client, the economically dependent.

In the previous section, we mentioned one of the peculiarities of this figure as in the contract termination, but this time we must speak further on what constitutes economically dependent workers (TRADE).

They are economically dependent independent contractors who:

- perform an economic or professional activity for profit;
- perform this activity in a usual, personal and direct way.
- work mainly for one person or entity, named Customer, and;
- perform their activity for a client or a company but still receive 75 percent of the working income of this activity.

Also, for the performance of economic or professional activity as economically dependent workers, it must cumulatively meet the following additional requirements:

- they must not be responsible for employees or contract or subcontract all or part of the activity with others, both in terms of the customer contract activity which depends economically as activities that could contract with other customers.
- they must not run their activity indistinctly with workers providing services under any form of recruitment provided by the customer.
- they must have their own production infrastructure and equipment necessary for the conduct of business and independent of their client, when in such economically relevant activity.
- they must develop their own activity organizational criteria, subject to the technical indications that his client could receive.
- they must receive a payment based on the result of their activity, according to the agreement with the customer and taking on risk and responsibility thereof.

g. Leased or Seconded Employees

As mentioned above, the working relationship established between the employer and the employee has a personal nature, that means that it is a very personal obligation, which cannot be transferred to a third party, partner, associate or employee not related to the employer for any legal connection.

However, independent contractors gather double circumstances of being independent contractors and entrepreneurs, with the possibility of hiring, in turn, other employed persons. This double circumstance determines the right of independent contractors to join unions either existing or to be established and also to join any of the existing business associations established or to be established, without prejudice to the possibility of self-employment associated specifically.¹⁰

Thus, Spanish case law has ruled that labor cannot be regarded as personal service delivery when substitution without the permission of the company is possible.¹¹

Therefore, the employed persons, to be subject to the guidelines of an employer

¹⁰ TCO 98/1985

¹¹ TS 6/10/17

cannot delegate its functions to another person or hire another worker; while independent contractors can give employment to employed persons.

However, it should be noted that the TRADE, this special form of independent contractors cannot be responsible for employees or contract or subcontract all or part of the activity with others, both in terms of outsourced activities with the client's economically dependent as activities that could contract with other customers.

h. Regulations of the Different Categories of Contracts

In Spain, there are a variety of employment contracts and all of them are properly regulated in the Statute of Workers. There is a common root that weaves all contracts, since they must follow certain general principles of law.

In terms of capacity, we can say that, those who can sign a contract are:

- the elderly (18 years).
- all children under 18 legally emancipated.
- over 16 and under 18 if they have parental permission or from whom it is responsible. If living independently, with the express or tacit consent of their parents or guardians.
- foreigners in accordance with the laws applicable to them.
- on the form, there is a principle of freedom of form, which means that it can be made orally or in writing.

Writing is mandatory when required by statute, and always in the contracts regarding:

- practices.
- training.
- to carry out a work or service.
- part-time jobs, fixed relay discontinuous.
- at home.
- workers hired in Spain for Spanish companies abroad.
- the term contracts which duration is longer than four weeks.

However, each party may require the agreement to be written, at any time during the course of the employment relationship.

The types of contracts can be further classified into two categories: indefinite contracts and temporary contracts. The first category includes part-time contracts (if the ratio is undefined), and ordinary and indefinite permanent employment promotion; the second group, all of the others.

In principle, any labor contract is permanent and full time, unless the employment contract states otherwise.

The rules governing each type of temporary contract, establish what the minimum and maximum duration of the contract is.

Furthermore, there are a number of common principles of temporary contracts, which are:

Exceptionally

The possibility of setting a term of relationship or hold a final term, exceptionally supported when justified by an objective reason, pointing out the legal provisions that

can hold fixed-term contracts in the event that the own specific standard, to cover temporary nature needs, and provided that, in the case, attend specifically the objective cause is to be held.

However, in Spain, this exceptionally has not prevented the excessive growth of temporary contracts. The significant weight of temporary workers (around a third of all salaried employees) is an anomaly in the European context, and has led to a strong segmentation between permanent and temporary employees.

Typicality

Contracting temporarily is limited to the legally regulated cases, existing in this field a reserve of law derived from the Constitution and an expressed authorization to the regulations to complement the legal regulation of the procedures laid down in the law.

Causality

In all of these contracts, the principle of causality is present as an element that defines and classifies. The temporary contract requires a cause that justifies it, that is, in Spain, temporary hiring is eminently causal.

Rules of necessary rights

The determination of the cases of temporary contract and its nature constitutes a rule of necessary rights core. Legal regulations authorize collective agreements to supplement the contents set by law, in the aspects that the effects are determined but cannot overlap the legally imposed limits.

As for the reference to civil law, note that as a general rule, in our system, the provision of labor for the production of goods and business services is subject to labor law and, therefore, qualifies as a juridical labor. The use of commercial or business figures to define personal activity services still remains an atypical formula to qualify the performance of work within a productive organization.

Therefore, the legal employment relationship arises from a bilateral legal business, the contract between the two subjects, worker and employer, who agreed to it.

Finally, as for the limits, it can be said that, although the employment contract is a regulated contractual relationship, there are two legal precepts of diverse origins and functions, which block the ability of the parties to the employment contract to alter the legal and conventional working and employment conditions in which you insert the worker performing the services in specific industry productive with a specific qualification.

i. On the one hand, the non-withdrawal rule provides for individual autonomy, less favorable conditions or simply anti - labor and employment regulations or conventionally fixed. The will of the parties specified in the employment contract cannot establish the prejudice of the worker, less favorable or contrary to the laws and collective agreements.

ii. On the other hand, the law imposes a principle of unavailability or inalienability of rights granted to workers imperatively by law or by collective agreement. The workers cannot validly use, before or after given, the rights that are recognized by rules of necessary rights, nor of those recognized as unavailable by collective agreement that extend to the transaction or waive of the rights recognized by rulings favorable to the employee, subject to the possibility of transaction within legal limits.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

In Spain, the workers' primary regulation, and situations of independent contractors, economically dependent autonomous workers, are regulated by the Law.

In addition, in the process of re-characterization of an independent contractor, one must also take into account the general principles of law. Indeed, the most widely used mechanism in the re-characterization is the individual autonomy of the parties who hire the services not subject to labor legislation. The provision of work under a labor contract has to be registered, but not for a civil or commercial one. Leasing of civil rules, commercial contracts or supply transport ones are contractual types and channel the work to a legal firm which excludes the application of labor law and prevents the owner of the company from having to be registered on the RGSS as an employee working for this employer. Normally, these operations are associated with productive decentralization scenarios outsourcing and professional services tend to frame new types of work arising from the society of services and information, both highly-skilled and poorly educated.

Individual autonomy and contractual documentation are the basic elements of such normally un-imposed re-characterization. Individual autonomy of the parties is to choose the type of relationship they both agree to engage in labor as including it in a civil or commercial contractual typology. The intention and the will of the parties directly regulate the content of the service and conditions govern it. Therefore, the content of the contract document expresses not only the specific content of the provision of work and the conditions under which it should be put into practice, but also, and very specifically, which established mandatory relationship between the parties is excluded from the rules governing wage labor, notably labor regulations, union activity and collective regulation of working conditions.

Clearly these operations, which at the time of establishment of the relationship of services excluded from consideration as labor, can cause a drastic reduction of rights for people. Nevertheless they should enjoy effective protection as workers. So, there is a possibility that these mechanisms will create a possible concealment of the existence of an employment relationship.

In short, it affirms the principle that we must address specifically how he handles the work performed for the production of goods and services in the company and not so much the content of the contract which sets the document signed by the parties as a way to qualify as providing work or outside work, which has been called the principle of primacy of reality in the qualification of labor relations. Spanish case law, consistent with this, has denied the parties the power to determine the nature of the relationship of services. It must be determined by the particular way in which the activity takes place,

which is both labor if it meets the characteristics of the employment contract described in the law. Therefore, the name that the parties give to their relationship is not binding on its nature, but it does not mean that in reality such provision cannot be defined as labor.

b. The Legal Consequences of a Re-Characterisation

In the first place, the false independent contractor should sue the employer to claim to be hired as a salaried worker by filing a claim for recognition of law to the Courts. In this situation, the false independent contractor has two possibilities: Sue the employer when he is still in the company or sue the employer since he was fired.

If the worker filing of the application while he was still in the company and finally got

to show the existence of an employment relationship, the employer would be required to register as indefinite with the salary he had been receiving, plus recognizing initial seniority.

However, if the worker files the application after he has been fired, and wins the trial, it will be recognized as the existence of an employment relationship and, therefore the contract termination would be classified as null or unfair.

In both cases, if the employee has obtained a ruling in his favor, the next step would be to sue the company before inspection work to pay their Social Security contributions in the last 4 years prior to the filing of demand.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Independent contractors who want to be recognized for the right to be employed persons in the trial will have to prove that there is an employment relationship and therefore, meet the characteristics of a contract of employment. This employment relationship exists when, for example, there is a specific schedule (holidays are taken, leave and rest, use of the technical and material resources of the employer and the services are provided under the direction and supervision of company staff).

First, the person who wants to be recognized as a worker should reflect the existence of an agency relationship, proving that some of the following factors concur:

The framework or hierarchical insertion into the company, the worker must follow orders, mandates and guidelines:

- subordination to the person or persons who have powers of command;
- submission to a schedule and appropriate disciplinary standards;
- monitoring which is subject to certain employees under the use of new technologies;
- monitoring of performance;
- control of timing;
- presentation of work;
- making regular reports to account the work.

Second, it must be proved that a number of signs that indicate that there is strangeness in the fruits and risks are concurring. Some of the common signs of alienation that could claim to prove the existence of an effective working relationship would include:

- to deliver or make available to the entrepreneur products made or services performed;
- the adoption by the employer of the decisions concerning market relations or relations with the public, such as:
 - fixing prices or rates
 - selecting clientele
 - indicating people to care
 - fixed or periodic character of labor remuneration
 - calculating the compensation or the main concepts under the same criteria that keep a certain proportion to the activity of the employer or the free exercise of professions.

Third, you should prove the remuneration for the provision of services, as Spanish law recognizes as worker just persons whose services, voluntarily rendered to another, natural or legal, are paid by it. The lack of wage determines the absence of labor contract "for lack of cause". However, it is not crucial how the remuneration is perceived: under invoices and documentation of commercial transport contracts and subject to VAT tax

regime or the regime implementing autonomous Social Security.¹² Neither the amount of the remuneration is a percentage of what the company bills the customer keeps its configuration as salary compensation.¹³

In labor law it is common to afford greater protection to the worker who is weaker party in an unequal relationship. This protection in such cases means that if there are several indications that the employment relationship is working, the company will have to fight the evidence, not with other circumstantial evidence.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

One of the damages that the employer who employs a worker as an independent contractor must bear, when in fact the provision of services between them is governed by an employment relationship, is to conduct un-prescribed contributions.

In addition, you must pay the Social Security penalties for having evaded the worker registration on the Social Security.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

To adequately justify the relationship of independent contractors, it would be necessary to conclude an agreement.

The contracts made in implementing autonomous professional activity may be written or oral. Each party may require from the other, at any time, the formalization of the contract written. The contract may be concluded for the execution of a work or series of work or to provide one or more services and the time agreed by the parties.

In addition, a worker who wants to register as an independent contractor must follow a few steps required to perform all independent contractors.

First, they have to register with the Tax on Economic Activities (IAE), as long as it is not exempt, within ten working days before the start of the activity. The Business Tax or I.A.E. is a tribute to local character, which taxes the exercise of business, professional or artistic exercised or not locally. It is mandatory for every company, business or professional.

Since January 2003, individuals and corporations are exempt from this tax, which have a net turnover of less than 1,000,000€. However, it is still mandatory to register on the tax.

For such processes, they must go to the tax authorities or the city council, and fill in the form 845 (for activities subject to quota municipal), the 846 and 850 (for the activities subject to provincial share) or 846 and 851 (for activities subject to national quota), and select the heading that corresponds to their business.

Once discharged from the IAE, the worker shall have a period of 30 calendar days from the start of the activity to register as self-employed in the administration of the Social Security Treasury.

Secondly, it would be necessary to apply to become a member of the Special Regime of

¹² TSJ Catalonia 25/01/93, TS unif doctrine 29-12-992

¹³ Teaching unif TS 12/29/99

Social Security for Workers Independent contractors (RETA), within 30 calendar days of the start of the activity.

The document to become a member of the Special Regime of Social Security of these workers, as well as general data, must contain those related to his business or occupation, and peculiarities regarding contributions and protective action.

The registration request is presented at the Provincial Administration of the Social Security or at the one which boundaries the establishment or, failing that, where he is domiciled.

The application to become a member of the Social Security, as the contribution, is unique, even if the worker develops several activities leading to their inclusion in the scheme. In these cases, if the employee elects to invoke the coverage of industrial accidents and occupational diseases, coverage for such contingencies is practiced by the activity that is applicable to the highest contribution rate among those included in the current premium rates. To this end, workers must make a statement of its activities to the Social Security Treasury in the application to become a membership.

Thirdly, you will need to register for census and taxation and choose accordingly. Thus, the employee must complete form 036 in which you opt for the relevant tax regime and indicate the activity that is to be performed and the data of the company, in addition to applying for an identification tax number (TIN). This process will have to be completed in any administration of the tax.

b. Day-to-Day Management of the Relationship

An independent contractor is an individual who routinely, personally, directly, on their own and outside the scope of management and organization of another person, performs a business or a professional activity for profit, whether or not he provides occupation for employees.

The independent contractor organizes his work without being subjected to a timetable, so that there is no subordination to the company. Moreover, he can work for one company or for several, but usually works for several.

Thus, the independent contractor does not receive instructions about how he has to do his job, in that, he is not subjected to the orders and directives of the company, since he can decide what work he wants to do and what he does not.

Finally, he perceives benefits for the service provided through bills, which may or may not be the same amount each month.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The new Government is about to create the Integral Law of Independent Contractors. This law, that aims to improve their labor legislation by making more reduced fees and increasing the social protection to them.

The new law aims to ensure that independent contractors whose real income does not exceed the threshold of the minimum wage are not required to pay to Social Security and that are established new formulas for the Social Security pay of part-time self-employed and non-habitual self-employed.

It also aims to achieve full compatibility between the receipt of a retirement pension and the development of a self-employed activity and for the self-employed to have the same social protection as ordinary employees.

The main measures to be taken by the law are as follows:

- increased flexibility to change the contribution base.
- new Social Security formulas adapted with specific fees for part-time self-employed and also for those who carry out the activity on a discontinuous basis or as a complement.
- payment of the fees adjusted to the dates of discharges and withdrawals in the Social Security.
- expansion of the flat-rate from 6 to 12 months.
- bonuses during pregnancy and after leaves for this reason.
- compatibility with the retirement pension.
- greater facilities for conciliation for economic dependency issues in cases of dependency care, maternity, or temporary incapacity; And bonuses for family care, periods of maternity leave, adoption, foster care, risk during pregnancy, risk during breastfeeding or suspension for paternity, as well as for self-employed women who return to their activity after maternity.
- deduction in the Personal Income Tax of the expenses that come from the automobile, the electricity and the water.
- delay of VAT income until the moment of payment to customers.
- smoothing penalties for late payment of fees, from an initial 3 percent to 20 percent currently applied for the delay; and deferrals in the payment of debts with Social Security.
- the new regulations will streamline the procedure by cessation of activity and increase its duration to match it with the unemployment benefit of employees. In addition, a cessation benefit will be created.

b. Recent Amendments to the Law

On October 10th 2015, the Law 31/2015, which modifies the regulations on independent contractors and encourages self-employment, entered into force.

This Act amends the Self-Employed Workers Statute (approved by an Act of 2007) and contains a number of measures to improve the situation of self-employed persons and to facilitate the implementation of self-employment initiatives. Its main new features are:

- limitation of the financial liability of the self-employed worker in respect of his/her debts (in line with the recent changes in Spanish legislation on bankruptcy).
- the possibility that so-called "Independent contractors economically dependent" (TRADE) can, in certain cases, hire workers (basically, in cases where the economically dependent self-employed worker needs someone to take his/her place when taking maternity leave or to care for relatives).
- a change in the composition of the Council for Autonomous Work, a body designed to promote institutional participation in this area.
- the reduction of social security contributions for workers who want to start an autonomous activity, especially for young people under 30 (men) or under 35 years (women) or if they are disabled or victims of gender violence or terrorism.
- compatibility between unemployment benefits and the income from self-employment in the case of workers who launch an autonomous activity (up to 270 days). This measure can also apply to the incorporation of the unemployed person into a cooperative or a worker-owned company. This new Act 31/2007 does not abolish the traditional possibility of receiving all accrued unemployment benefits

in a single payment if that amount is used to launching an autonomous activity (an operation known as “capitalisation”).

- the Law allows the capitalisation of economic benefits due to the termination of the self-employed worker’s activity (equivalent to unemployment benefits for self-employed persons) when the worker proves that this amount will be used to launch a new activity (on an individual basis or within a cooperative society or a worker-owned company).
- the Act reduces the social security contributions of the spouse and relatives of self-employed persons who work in the business.
- the Law also reduces the Social Security contributions for cooperatives and temporary agencies that incorporate self-employed (unemployed) persons as partners. Act 31/2015, of 9 September 2015 on self-employed workers.

Suggestions based on Specific Cases

In this section, we will discuss the same case viewed from two different perspectives in order to distinguish the difference between an independent contractor and an employee.

A Company that sells pets requires the services of a veterinarian to care for their animals:

Scene 1

The Company has a contracted worker who is registered in the General Regime of Social Security, and goes every day to the facility to supervise the status of animals. He has a schedule of 9:00 to 15:00, and in the event that an animal become seriously ill, he has to assist it after hours, charging extra for extra time worked. If he cannot go, the Company does not allow him to send someone else in his place. The Company pays him 1.300€ per month (twelve payments) and he has a one month vacation.

Firstly, we can say that, he obeys the dependency note, considering that the worker is subject to the organization of the company, which determines when the services are provided and establishes the holidays, and also the fact that he goes to the place of work of the Company every day.

Secondly, the worker receives a monthly salary, which is why, in this case, he obeys the requirement of payment.

Thirdly, the job reverts to the Company and the worker only receives an economic payment without assuming economic risk.

Finally, we can say that, there is an employment relationship between the employee and the Company, since all the requirements of a contract are done, so in this case, the contracted worker is an employee.

Scene 2

The Company has a contracted worker who goes to the facilities of the Company once a week, when he decides it, or sometimes when there is a serious case, or if the company asks for him. Besides providing his services to this Company, he works for three companies in a more permanent fashion. From each of these companies, he charges 400€ per month, however, there are months that he also provides services to other companies.

Firstly, the employee organizes the work and decides when go to the Company, according to the needs of the client, which does not obey the dependency requirement.

Secondly, receives compensation for the service rendered, but this is not his only or principal income. Also, this payment is not fixed for himself, but for the realization of a service.

Thirdly, the worker decides whether to accept the work and the volume thereof, being for him all the profits, so in this case, the condition of alienation is not carried out.

Finally, we can say that there is no employment relationship between the employee and the Company, considering that, the features of a contract are not obeyed. This is the reason why, in this case, the contracted worker is not an employee.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

It will be stated that a person or an entity operating through a permanent establishment in Spanish territory:

- when he acts in Spain, in any capacity and continuously or habitually, facilities or workplaces of any kind in which he performs all or part of the activity.
- when he acts in Spain through an agent authorized to contract on behalf of the non-resident, provided that such powers are habitually practiced.

Specifically, permanent establishments are considered every place of management, branches, offices, factories, workshops, warehouses, shops or other establishments, mines, oil or gas, quarries, farms, forestry or livestock or any other place of extraction or exploitation of natural resources and construction, installation or assembly project which existed for more than six months.

When a taxpayer has various centers of activity in Spanish territory constituting different permanent establishments, each of them should be named differently and if it is a legal entity it must also obtain a different tax identification number for each permanent establishment.

Thus, we see how the concept of “permanent establishment” is not strictly linked to the provision of services by an autonomous, since it can provide its services with or without the existence of a permanent establishment.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

Spanish law provides a general definition of what a Permanent Establishment is. In this way, a permanent establishment is defined as a fixed place of business through which an enterprise is wholly or partly carried on.

As noted in the comments to MCDI, the following three notes are to be given in the general definition of Permanent Establishment:

- the existence of a “place of business”
- the place of business must be “fixed” and,
- through this place of business must be “conducted business activities”.

The Committee of the Organization for Economic Co-operation and Development (OECD) of Fiscal Affairs considers the term “place of business” to include any premises or facilities to be used for the realization of economic activity of the company, whether or not exclusively used for this purpose. Note that for there to be a place of business would be enough to have a space available for the development of the activity. In this sense, it is irrelevant whether the use of the premises is done as the owner or lessee.

Moreover, it would not even require the existence of any legal right of use on the space used so you can come to understand that there is a permanent establishment because, as just noted, what is truly important is the effective and simple arrangement of a certain physical space for the development of the activity.

The term “place of business” is thus a term that can encompass diversity of possibilities, from the traditional offices to spaces as would be located in a business center. Also included in this term, is the space that could be given by a company to another of their group who were not resident in the development of the activity of the latter, but this assignment was free and was not formalized in a contract.

VII. CONCLUSION

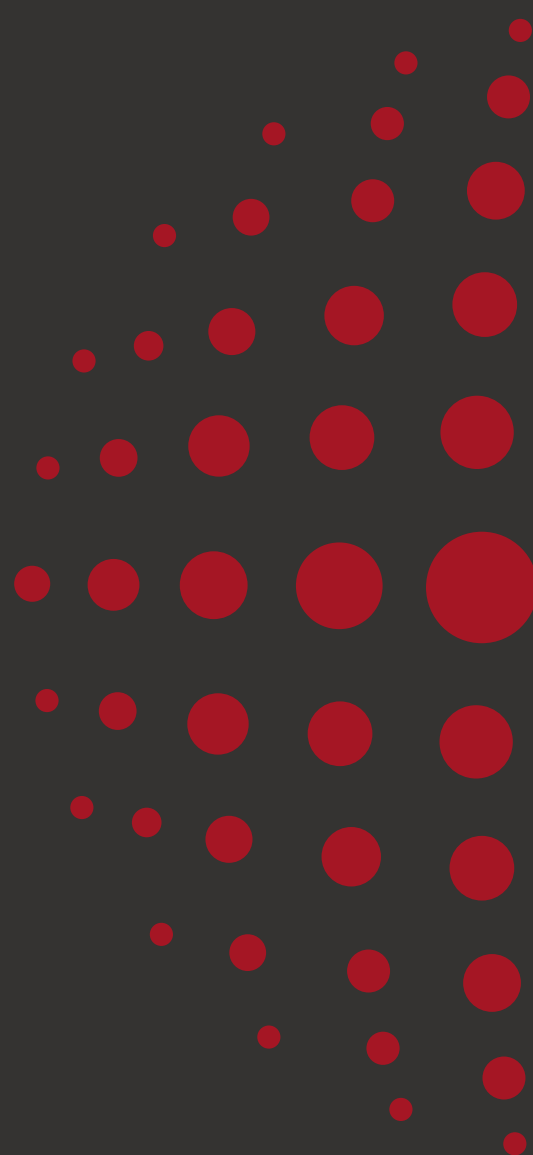
Sometimes, it is very difficult to make the difference between an independent contractor and an employee, as the employer hires workers registered as self-employers when in fact there is an employment relationship between the worker and the company.

The solution to determine which is which, an independent contractor or an employee, is analyzing the characteristic features of a contract of employment, which are: dependency, alienation, personal nature of the relationship, compensation, and exclusivity and assiduity.

These factors are those that enable the qualification and delivery of services as labor and, consequently, if there is no submission, the contract may be considered civil or commercial, but never as a labor one.

Finally, encourage people who are in this situation to be hired as freelancers when in practice there is an employment relationship to sue the employer, by taking into account that the document signed by the parties does not matter, for the really important thing is the reality in the qualification of the employment relationship. Therefore, if the relationship between the worker and the company obeys the characteristics of the employment contract, the employment relationship will be judicially qualified as a labor one.

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SWEDEN

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I. OVERVIEW

a. Introduction

In Sweden, the differences in terms of protective legislation for employees compared to independent contractors are rather significant. The legislation considering employees and employment is extensive while standard civil- and contract law applies for a relationship between a company and an independent contractor. The characterization of the contract is made by an overall assessment of the circumstances. Hence, a re-characterization may have significant legal consequences.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

The difference between an employee and an independent contractor in Sweden is based on whether or not the person performing a work task is determined to be an “employee” according to Employment Protection Act (Sw. *“lagen om anställningsskydd”*). Similar definitions are relevant for tax treatment and benefit entitlements. The legal concept of the term “employee” is peremptory and the meaning is determined by case law. According to case law, an overall assessment of the objective circumstances has to be made in each individual case. The following factors are usually considered to be characteristic of the existence of an employment relationship between a company and a person:

- the work is performed by a single person. The person is not entitled to independently hire helpers.
- the company is responsible for providing the work equipment.
- the person is bound by specific directives and instructions issued by the company.
- the person is obliged to perform work when the company requires.
- the remuneration for the work performed consists of a guaranteed salary (at least partly).
- the company compensates the person for direct expenses (e.g. business journeys, entertainment).
- the relationship can be described as a long lasting legal relationship.
- the person is prevented from performing similar work for someone else.
- the person is equal to an employee, both socially and economically.

The opposite conditions indicate a relationship of an independent contractor and a company. If the person performing work for the company previously has been employed by the company, it is normally required that an actual change of the working conditions is at hand in order for the person to be considered as an independent contractor. As such, it is normally not possible for a former employee to continue to perform exactly the same working tasks as an independent contractor.

Even if a consultancy agreement formally has been entered into by a legal person, such as a limited liability company or other, there is a risk that the agreement is seen as a contract of employment between the underlying physical person and the company. However, if the agreement has been entered into by a limited liability company (“Sw. *aktiebolag*”) this constitutes a factor that substantially indicates that no employment relationship is at hand. Further, if the consultant that is party to a consultancy agreement is registered for F tax in Sweden, i.e. liable for the payment of taxes and social security contributions for performed work, such a factor normally indicates that the relationship is in fact a consultancy relationship. However, if it can be proven that the aim of the agreement is to evade mandatory law, such a factor could strongly suggest that an employment relationship is in fact at hand.

b. General Differences in Tax Treatment

Someone who pays compensation for performed work is obligated to deduct preliminary taxes from the compensation. This applies for physical as well as legal persons. If an independent contractor is registered for F tax this entails that the contractor is responsible for his or her own preliminary tax deductions.

As regards contributions for social security ("*Sw. arbetsgivaravgifter*"), such shall only be paid in the case of compensation for work performed by physical persons. Work that entails a right to receive salary can never be performed by legal persons. If an independent contractor is registered for F tax this entails that he or she is responsible for the social security contributions.

Consequently, a company is obliged to pay social security contributions for its employees and to withdraw preliminary income taxes on the remuneration paid. Further, in spite of what is stated above regarding F tax, a hiring company can be responsible for taxes and social security for a contractor if the approved F tax registration is revoked. Further, the hiring company can be responsible for taxes and social security contributions if it is obvious that the work is performed under such circumstances that the person performing the work is to be considered an as employee and the company has not reported this do the Swedish Tax Agency (*Sw. "Skatteverket"*). In such case the Tax Agency can declare that the hiring company and the consultant shall be jointly liable to pay social security contributions.

c. Differences in Benefit Entitlement

The existence of an employment relationship imposes obligations on the employing company to pay vacation benefits, sick pay, overtime compensation etc. while an independent contractor is responsible for paying or covering such benefits.

d. Differences in Protection from Termination

Independent contractors are not protected from termination – their rights related to termination are solely based on what is agreed between the parties.

As regards employees, there is extensive protective legislation laid out in the Employment Protection Act. A dismissal must be based on objective grounds. Objective grounds are not defined by statute or case law, but can be either for objective reasons or subjective personal reasons. Objective reasons are dismissals based on redundancy, re-organization or the economic situation of the employer, while subjective personal reasons are all dismissals that relate to the employee personally, such as the employee's conduct or performance.

An overall assessment of all the factors involved must be made when determining whether objective grounds for dismissal are at hand. The employer has the burden of proof in this regard and it can be quite difficult to present sufficient evidence to support a dismissal based on personal reasons. For instance, in a situation when an employee is not performing as well as the employer demands, the employer has an obligation to provide support to the employee in order to help him/her to improve.

A dismissal with notice will never be considered based on objective grounds if there were other alternatives available to the employer, such as relocating the employee elsewhere within the business. Further, the employer must observe certain rules set out in the Employment Protection Act when serving a notice of dismissal to an employee.

The procedure for dismissing employees due to subjective reasons is laid down in the Employment Protection Act and varies to some extent depending on whether the dismissal is due to objective reasons or subjective personal reasons. Prior to dismissing an employee due to objective reasons such as redundancy, the employer may be obliged to conduct consultations under the Co-Determination Act ("*Sw. lagen om medbestämmande i arbetslivet*") if the employer is bound by a collective bargaining agreement or if the employee is a member of a trade union.

e. Local Limitations on Use of Independent Contractors

There are no statutory limitations on the use of independent contractors. However, a trade union may, under certain circumstances and if the company is bound by a collective bargaining agreement, have a right to consultations with the hiring company before it engages the independent contractor. Further, the trade union may have a right of veto if the company's planned action is in conflict with what is generally accepted within the applicable collective bargaining agreement's area.

f. Other Ramifications of Classification

In principle, it is irrelevant whether the person is referred to as an employee or a consultant in the agreement. Instead it is the degree of independence from the hiring company, which is decisive.

g. Leased or Seconded Employees

The use of temporary work agencies is regulated in the Hiring out of Temporary Staff Act (*Sw: lagen om uthyrning av arbetstagare*). The temporary work agency is obligated to, during the period of the leasing of an employee to a client company, to ensure the employee the fundamental working conditions and terms of employment (regarding salary, working hours, overtime, breaks, holidays etc.) that applies for the client company according to applicable collective bargaining agreements or other binding general rules. Further, it is prohibited for the agencies to stop the employee from taking up employment with the client company. The client company is obliged to inform the temporary worker regarding any vacant positions that may be available at the client company. The temporary work agency as well as the client company can be liable to pay damages to the employee for violations of the aforementioned act. Furthermore, an agreement that violates the employee's rights according to this act is invalid. However, it is possible to deviate from certain parts of the act by a central collective bargaining agreement.

h. Regulations of the Different Categories of Contracts

The different groups of contracts are defined by mandatory legislation in regards to employment law, tax law and social benefits law. If an individual is not considered to be an "employee", the relationship is regulated by the general civil law.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As stated above, the legal concept of the term "employee" is peremptory and the definition is set out in case law. Similar definitions are relevant for employment law, tax treatment and benefit entitlements. Hence, an independent contractor can be re-characterized, in a legal sense, as an employee based on the criteria listed above.

b. The Legal Consequences of a Re-Characterisation

As previously mentioned, the legal consequences of a re-characterization are significant. For instance, if an independent contractor is considered to be an employee, the termination of the contract must be based on objective grounds, the contracted person will have a right to vacation pay, overtime compensation and other employee benefits. The employee may also be entitled to retroactive vacation pay, overtime compensation and other benefits. Further, if the company is bound by collective bargaining agreement consequences with regard to the trade union might arise since the hiring of the independent contractor can entail a violation of the provisions in the collective bargaining agreement regarding working hours, salary etc.

The fiscal impact can entail that the company becomes responsible for preliminary tax deduction and for social security contributions. With regard to taxation this also applies for a limited liability company without F tax registration. Moreover, there is a risk that the contracting company is awarded a fiscal penalty if it has not fulfilled an obligation to make tax deduction and has presented incorrect data to the Tax Agency. Also the consultant can be awarded a fiscal penalty in the same situation.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

A consultant needs to go to court with his/her claim that he/she is an employee in order to be able to have success with such an interpretation. This is often a long, expensive and difficult path to follow and will in principle only occur when the parties disagree on how, when and on what basis the contract can be terminated, or the parties disagree on the right to remuneration.

As regards fiscal concerns, the Tax Agency can also by perusal ("*Sw. genomsyn*") establish that an underlying physical person in a consultancy services company in a legal tax sense is to be regarded as an employee.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

If an independent contractor is re-characterized as an employee, this may entail that the hiring company violates the Employment Protection Act, Co-Determination Act or other related employment legislation. In such case, the employee may be entitled to general and economic damages for these violations. In addition, a trade union can also be awarded general damages for such violations where applicable.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

First and foremost, to avoid the risks of re-characterization of an independent contractor to an employee, it is preferable that the contracting party for consultancy services is a limited liability company that is registered for F tax. Further, it is important that the independent contractor is actually independent from the hiring company, e.g. that the contractor performs work for other hiring companies and that the contractor uses its own equipment. In a consultancy agreement it is important to define the task or assignment and how the work should be performed. Moreover, the registration for F tax should be an essential condition to the agreement.

b. Day-to-Day Management of the Relationship

It is of importance in the day-to-day management of the relationship to respect that the contractor is not an employee and thus is not supposed to be instructed as if an employment relationship was at hand. It is also of relevance how remuneration for the results is handled, e.g., the invoice could preferably be based on the delivery of the assignment, or hours of work performed, rather than be based on a fixed weekly/monthly fee. Further, if possible, it is preferable to allow the contractor to perform work for other principals in addition to the company. In the case of a re-characterization, the course of the day-to-day management may be even more important than the written contract.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

The use of independent contractors is increasing in Sweden. Hence, the acceptance of its presence as a complement to regular employees has grown in the legal context. Another new trend on the Swedish labour market is the increasing number of self-employment companies and self-employed persons. This arrangement is basically that a person is employed by a self-employment company and is then either hired out to businesses for a period of time or for a specific assignment. It is the self-employed himself/herself who obtains the assignments. The self-employment company invoices the hiring/contracting company for the performed assignment. Salary and social security contributions are paid by the self-employment company to the self-employed person based on the invoiced amount. Thus, the contracting company and the self-employment company are the contracting parties.

However, trade unions and representatives of the temporary work agencies on the Swedish labour market have criticized the self-employment arrangements and argues that its use constitutes a circumvention of the peremptory concept of the term "employee". The arrangement has not yet been tried by a court in Sweden.

b. Recent Amendments to the Law

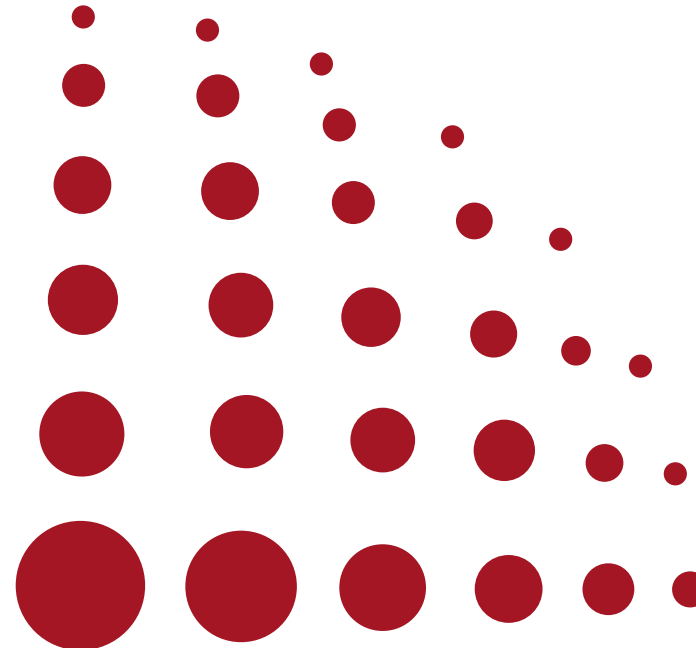
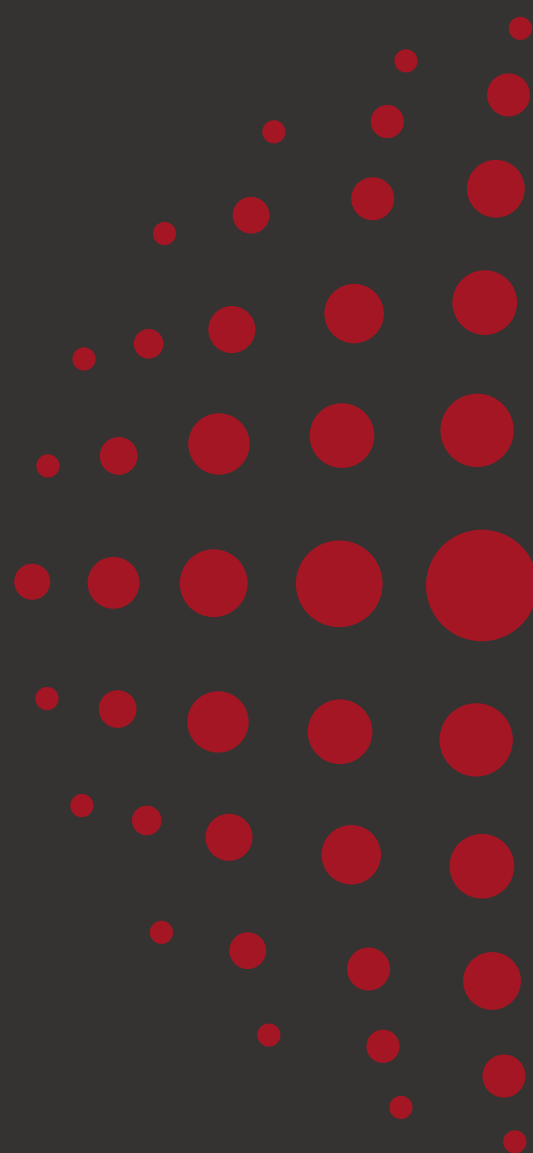
In a case from the Labour Court from 2012 (AD 2012 no. 24) a consultant was re-characterized as an employee. A public service radio company had contracted a person as anchorman through her sole proprietorship. The person had previously been employed in different temporary employments at the company. The Court stated that given that the person had previously been employed by the company, an actual change of the working conditions was required in order to regard the person as an independent contractor. The Court concluded that the only real change since the new arrangement was the practice of payments by invoices instead of regular salary payment. Further, the invoiced amounts were at approximately the same level as the salary levels for employees in general at the company. The Court found that the working conditions had not changed in any material way and established that the relationship was in fact an employment relationship. The Court found that the person was to be considered to be a permanent employee and she was awarded damages for the company's violation of the collective bargaining agreement. No further compensation or accrued vacation pay etc. was awarded.

VI. CONCLUSION

In conclusion, Swedish law has a dynamic concept of the legal term "employee". Therefore, it is of importance to be careful when utilizing independent contractors to avoid a re-characterization to an employment. An overall assessment of the objective circum-

stances has to be made in each individual case in order to establish if the relationship is in fact an independent contractor relationship. The abovementioned factors should be taken into consideration when making this assessment. To be on the safe side, consultancy agreements should be entered into with limited liability companies that are registered for F tax. Yet, the field is developing. In the recent decade, new concepts have arrived in terms of alternatives to the regular employment, such as leased employees and self-employed persons, which may make it easier to engage independent contractors in the future.

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SWITZERLAND

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I. OVERVIEW

a. Introduction

In Switzerland, as in many other jurisdictions, the distinction between an employee and an independent contractor is of high practical significance, as different rules apply to each category regarding protection rights, social security and taxation. As statute law only provides basic guidelines on the distinguishing characteristics of each category, the decisions made by the Swiss courts in this area are of great importance. It is important to note that there are two different angles from which the question may be approached. On the one hand, there is the legal qualification of a contractual relationship for private law purposes (or in case of civil servants, public law), which determines whether employment law protection rights apply or not. On the other hand, employment status for social security purposes is regarded separately. For social security purposes, offering work to another business partner may qualify as a self-employed activity or as employment, depending on certain assessment criteria; these criteria are not identical to the criteria, which apply for private law purposes. Hence, in exceptional cases, a person offering her or his services may qualify as an independent contractor for employment law purposes, but as a dependent employee for social security purposes.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Generally speaking, the main factor which distinguishes an independent contractor from an employee under Swiss law is subordination. Whether a subordinate relationship can be accepted or not is decided by a holistic assessment of each individual case. It is necessary to check whether the person obliged to perform the work corresponds more to an employee or to a self-employed person. For this purpose, certain principles have been developed in doctrine and practice, so that there a number of factors which are taken into account in order for determining the existence of one or other contract. Material characteristics indicating an employment relationship are:

- high degree of directionality;
- subordinate to other persons serving the principal/employer;
- acting in the principal's/employer's name and for the principal's/employer's account;
- fixed working hours, working time checks, duty to regularly appear in the office;
- obligation to provide the entire workforce as well as the intensive use by the principal/employer;
- allocation of a work place;
- provision of work equipment or material by the principal/employer;
- agreement of a probationary period;
- granting of holiday by the principal/employer;
- conducting a personal file by the principal/employer;
- periodic remuneration;
- principal's/employer's business risk;
- agreement on non-competition; and
- expressly declaring the intention to establish an employment relationship.

Formal criteria that have only secondary importance are:

- payment of social security contributions by the principal/employer; and
- tax or social insurance deductions as if it was income from dependent employment.

Factors that indicate against the existence of an employment contract are:

- lack of subordination;
- possibility to terminate the legal relationship at any time;
- limitation of the workload to a specific work-related work and, consequently, to a shorter period; and
- provision of materials and tools and insurance of the risks by the principal/employer.

b. General Differences in Tax Treatment

The differentiation between an employee and an independent contractor has consequences with regard to social security law and tax treatment.

Social security law

Swiss social security is split into three 'pillars', each with its own characteristics and goals that help retired people continue to finance their way of life after retirement. Employers participate in the funding of most types of insurance with the exception of health insurance, which is financed by each insured person who pays premiums based on their age and where they live. The three pillars of the Swiss social security system are: Old Age and Survivors /Disability Insurance, an occupational pension plan, and private investment options.

First pillar

The first is a state pension plan that consists of various insurance schemes such as the Old Age and Survivors Insurance (OASI), Disability Insurance, and Unemployment Insurance. OASI and Disability Insurance are mandatory for all Swiss residents, be they employed or self-employed.

Second pillar

The second pillar is based on occupational pension plans and accident insurance. Employees who earn more than CHF 21,150 a year are automatically insured by a second pillar pension fund. When combined with the first pillar benefits, a person could expect to earn about 60% of their final salary after retirement to help maintain their standard of living. Self-employed persons may optionally contribute to second-pillar schemes but are not required to do so.

Third pillar

The third pillar is a private, individual option that workers can use to help make up the remainder of their income not covered by the first two pillars. Such schemes are also protected by law and often offer tax advantages. These typically take the form of a retirement savings account (with tax breaks) or a flexible savings account (few if any tax breaks).

Tax law

Both employees and independent contractors have to declare their income and pay income tax. Self-employed persons can deduct their professional expenses from income completely, while such deductions are not available to employees.

The services of an independent contractor are generally subject to VAT, provided that the annual turnover exceeds CHF 100,000.

c. Differences in Benefit Entitlement

By virtue of Swiss statute law, an employee is entitled to certain benefits, whereas an independent contractor is not. Benefits, which employers are entitled to are listed below;

Paid holiday leave

Unlike self-employed persons, employees are entitled to at least 20 days' paid holiday leave per year (based on full-time salaried employment).

Wage continuation

Where the employee is unable to work due to personal circumstances beyond his control, such as illness, accident, legal obligations or public duties, the employer must pay him his salary for a limited time, including fair compensation for lost benefits in kind, provided the employment relationship has lasted or was lasted longer than three months. Subject to longer periods being fixed by individual agreement, the employer must pay three weeks' salary during the first year of service and thereafter the salary for appropriately longer periods depending on the duration of the employment relationship and the particular circumstances. The employer has the same obligation in the event that an employee becomes pregnant. A written agreement, standard employment contract or collective employment contract may derogate from the above if it provides the employee with at least an equivalent benefit. In fact, many companies provide more advantageous benefits by written agreement, such as insurance providing a benefit of at least 80% of salary for up to 720 or 730 days' sickness absence. If employers chose to enter into such an insurance contract, they have to bear at least 50% of the insurance premiums.

Independent contractors do not benefit from this statutory protection. They may, however, enter into a private insurance contract providing continuation of salary in case of sickness for up to 720 or 730 days. They have to bear the full costs for such insurance coverage themselves.

Accident insurance

Employees have to be insured by law against accidents by their employer, whereas independent contractors have to take out their own accident insurance.

Unemployment insurance

All employees in Switzerland who have not yet reached retirement age are insured against loss of employment. Contributions are split between the employer and the employee. To receive payments, the following conditions must be met. The individual must:

- have been employed for at least 12 months within the two years prior to requesting benefits;
- have Swiss residency and a work permit;
- be registered with the regional unemployment office; and
- be actively looking for a job.

Unemployment benefits typically amount to about 70% of the average wage over the last six months to a year. Average wages are capped at CHF 12,350 a month. Insured persons with children may receive 80% of their average salary.

There is no unemployment insurance for self-employed workers.

d. Differences in Protection from Termination

There are substantial differences in the legal protection given on termination of an independent contractor's contract and that of an employee's employment. However, as it is a principle of Swiss employment law that either party can terminate an employment contract without any specific reason, the difference may not be as extensive as in other jurisdictions. In a nutshell, termination of an employment relationship is always subject to the agreed notice period, apart from when an employment relationship is terminated for a valid reason with immediate effect. If an independent contractor relationship qualifies as a mandate within the meaning of the Swiss Code of Obligations, a notice period

does not apply even if agreed between the parties. There are, however, certain statutory restrictions regarding the termination at an inopportune juncture.

Notwithstanding that an employer may terminate an employment contract without specific grounds, the Swiss “Code of Obligations” lists a number of reasons which render termination unfair. Under the Code, a dismissal is deemed abusive if issued:

- due to a quality inherent in the personality of the other party (such as relating to gender or race), unless such quality relates to the employment relationship or significantly impairs cooperation within the enterprise;
- because the other party exercises a constitutional right, unless the exercise of such right violates a duty of the employment relationship or significantly impairs cooperation within the enterprise;
- to prevent the other party from asserting contractual claims arising out of the employment relationship (such as rights under a contractually agreed settlement);
- because the other party asserts in good faith claims arising out of the employment relationship; and
- because the other party performs compulsory Swiss military service, civil defence service, military women’s service, or Red Cross service, or a legal duty not voluntarily assumed.

The notice of termination of an employment relationship by the employer will also be considered abusive, if it is given:

- because the employee belongs or does not belong to an employee association, or because he lawfully exercises a union activity;
- during the period the employee is an elected employee representative in a company institution or in an enterprise affiliated thereto, and, if the employer cannot prove that he had a justified motive for the termination; and
- in connection with a mass dismissal without prior consultation with the employees’ representative body or, if there is none, the employees (Art. 335f).

In cases of unfair dismissal, an indemnity payment equivalent to six months’ wages is required. This allows for additional claims for damages based on other legal grounds to be made.

Moreover, the employer cannot terminate an employment contract at an improper time. Upon expiration of a probation period, the employer must not terminate the employment relationship:

- during the other party’s performance of compulsory Swiss military service, civil defence service, military women’s service or Red Cross service and, where such service lasts more than twelve days, during the four weeks prior to and after the service;
- during any period of protected sick leave (where the employee is prevented from performing his work fully or partially through no fault of his own due to illness or accident): 30 days in the first year of service, 90 days from the second year of service until the fifth year of service, and 180 days from the sixth year of service;
- during pregnancy and during the 16 weeks following birth; and
- during the employee’s participation with the agreement of the employer at a foreign.

A notice of termination rendered at an improper time has no effect: the notice is null and void.

e. Local Limitations on Use of Independent Contractors

There are no limitations on the use of independent contractors in Switzerland.

f. Other Ramifications of Classification

Other ramifications of the distinction between employees and independent contractors mainly relate to their scope of protection during the contractual relationship. For example, safety regulations provided by the Federal Labour Act and by the Federal Law on Accident Insurance are only applicable to employees. Also, employers must abide by working time regulations for their employees, which do not apply to independent contractors.

g. Leased or Seconded Employees

The leasing of employees is a very common way for Swiss companies in need of temporary staff to avoid any discussions relating to the complex differentiation between employees and independent contractors. Swiss labour leasing law applies to all placements, both temporary and permanent, of personnel in Switzerland and imposes several key rules:

- a foreign labour-leasing company (e.g. agency, consultancy) may not place personnel at the premises of a Swiss end-user client;
- a Swiss labour-leasing company may only place personnel at the premises of a Swiss end-user client if in possession of a valid Swiss labour leasing licence; and
- a Swiss company may not use a foreign labour-leasing company to provide personnel.

These rules are strict and unambiguous and mean that foreign agencies wishing to do business in Switzerland are left with only two options: open a local office and obtain a labour-leasing licence, or make use of a local partner. While the former option seems preferable, there is considerable cost involved: other than the initial investment in opening a new office, the process of obtaining the labour-leasing licence itself is far from cheap and the recent strength of the Swiss franc means running costs are higher. A critical mass of business must be reached in order to make it a viable option. The latter option, on the other hand, requires a high level of trust, as the local partner will often be a recruitment agency itself. In addition there is a ‘Catch 22’ associated with an arrangement with a local partner because, as a Swiss company, it may fall foul of the ban on recruiting via a foreign labour-leasing company.

It is important to ensure that the supplier of the workforce is in possession of a valid permit. Companies in breach of Swiss labour-leasing law could be fined: the Swiss authorities will pursue Swiss companies first (typically the end-user client) and then any foreign companies found to be in breach. The contractor or employee will not usually be held liable for breaches unless they are deemed to be a principal of a company involved (director or owner of a foreign limited company working in Switzerland on contract, for example) and/or unless they are not complying with local tax and social security regulations.

h. Regulations of the Different Categories of Contracts

In Switzerland, employment relationships are governed by specific protective regulations, which are stipulated both in private and public law. The contract with an independent contractor normally qualifies as either a “mandate” (Auftrag) or as a “service contract” (Werkvertrag). Both of these categories are solely based on private law regulations that do not provide special protective measures for the independent contractor.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As with most jurisdictions, Swiss law upholds the following principle: when assessing the form and terms of a contract, the true and common intention of the parties must be ascertained without dwelling on any inexact expressions or designations they may have used either in error or by way of disguising the true nature of the agreement.

Hence, the re-characterization as an employee depends on the aforementioned several criteria, which have been developed by Swiss courts in conjunction with the few statutory law provisions on the issue.

b. The Legal Consequences of a Re-Characterisation

In the event of a re-characterization, the employer faces wide-ranging financial risks. The contractor may claim he is employed by the principal/employer, thus gaining the status of an employee, including any and all applicable benefits and protection rights.

In particular, the employee may retroactively claim compensation for accrued holiday, overtime, pension contributions etc. The consequences for the employer can be devastating in cases where the presumed independent contractor suffers a serious accident and is not properly insured against its consequences.

It goes without saying that in the case of a re-characterization, all protection rights in connection with the termination of employment apply.

Moreover, the employer will be retroactively obligated to pay social security contributions for the re-characterized employment relationship. This obligation covers the entire duration of the re-characterized employment relationship and is only limited by the applicable statute of limitation, which is five years.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

Persons seeking "employee" status can submit a respective claim with the competent labour court requesting the defendant to apply Swiss employment laws to the contractual relationship. At the same time, or alternatively, they can request a formal decision with the competent social security authority regarding their social security status (independent or dependent worker).

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

In the event of re-characterization, the employer must pay the outstanding social security contributions for up to five years plus late payment interests. The company organs (including the board members) are jointly and severally liable for the payment of the social security contributions for the first pillar (Old Age and Survivors Insurance).

Criminal charges due to deliberate breach of mandatory protection rules (e.g. in connection with work time regulations) are possible but only in exceptional cases awarded.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Although it is not necessary under Swiss law for a contract for services to be in writing, it is recommended for evidential purposes. Such contracts should reflect the most typical characteristics of an independent contractor relationship, such as:

- no exclusivity;
- no specific instructions on work time, place of work etc.;
- no paid leave;
- no provision of materials and work tools; and
- no provision of an office at the principals' premises.

b. Day-to-Day Management of the Relationship

When managing the contractual relationship with an independent contractor, it is important to observe the discussed criteria and to demonstrate that the independent contractor is not integrated into the principal's business organisation.

V. TRENDS AND SPECIFIC CASES

The Swiss insurance agency "Sucva" has recently classified Uber taxi drivers as employees rather than as freelance contractors.

The Sucva's decision was based on the drivers' inability to set price or payment type, and because the agency are threatened with consequences from Uber if they do not fulfill its requirements.

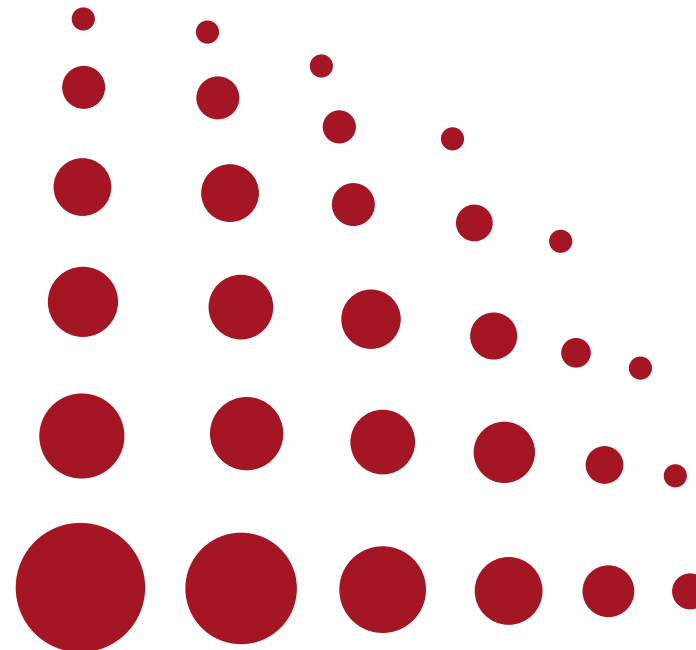
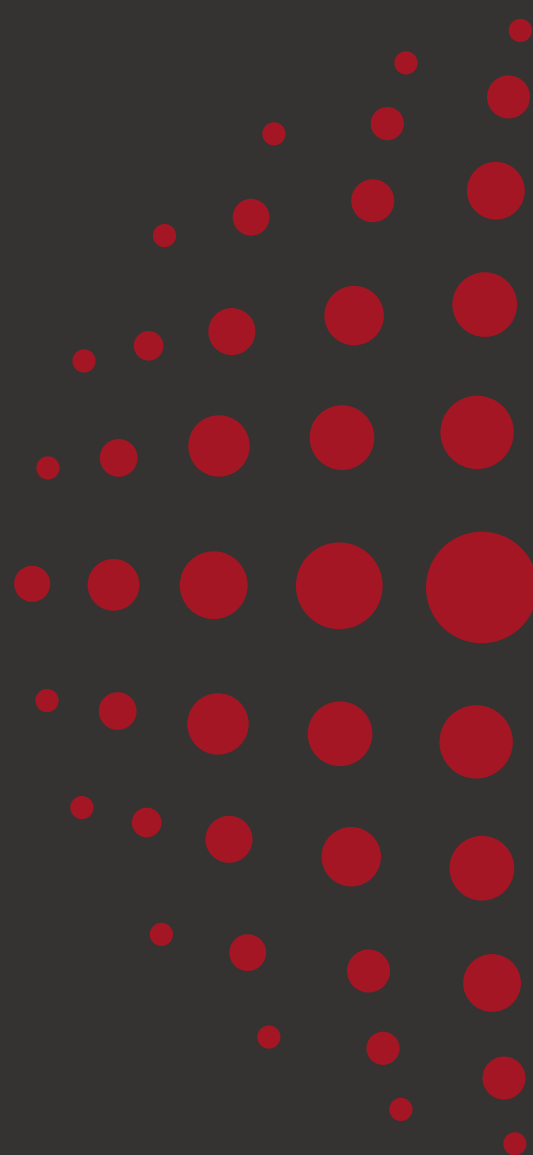
The Sucva described its decision on the classification as a "clear conclusion". The public sector insurer, which provides compulsory on-the-job accident insurance that is required for certain high risk professions, is involved in determining whether workers are freelance or not.

Uber has announced that it will challenge the verdict.

VI. CONCLUSION

When making the decision whether to have certain tasks within its business operation fulfilled by its own staff or by external workforce, a business should be aware of the possible consequences of a situation where a presumed independent contractor might be re-characterized as an employee. If choosing to take on an independent contractor, it is advisable to structure the contract in a way that mitigates the risks of a re-characterization. Alternatively, such risks can be avoided through the use of a licensed professional staff supplier.

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UNITED KINGDOM

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I. OVERVIEW

a. Introduction

In the United Kingdom, "employees" benefit from greater protection in law than independent contractors. These protections include, for example, the right to not to be unfairly dismissed, the right to redundancy pay and the right to maternity leave, paternity leave and shared parental leave. Employers and employees are also under certain duties and have rights under the health and safety legislation.

In the United Kingdom, there is a wider category of labour known as "workers" who only benefit from some of the protections, which are afforded to employees. Some of these protections are derived from statute (and in some cases, European law) and include for example, the right to holiday pay, the right to rest breaks, the right not to suffer deductions from wages, and national minimum wage. To be an "employee" or a "worker", there must be a personal obligation to execute the work in question, but the term "worker" is defined more widely than "employee" so that it includes certain types of independent contractors, home and casual workers. All employees fall within the definition of "worker" but not all workers will be employees.

Disputes may arise when an individual asserts a particular right in circumstances where the employer has previously designated the individual as an independent contractor (commonly requested rights include the right to holiday pay and the right not to be unfairly dismissed). The distinction between "employee", "worker" and "independent contractor" is therefore of critical importance to determine the level of protection afforded to the individual in question, as well as the obligations on the employer.

Equally as important are the tax implications of the status in question. The UK tax authority, HM Revenue & Customs (HMRC) distinguishes between self-employed labour (independent contractors who are genuinely pursuing any profession or business activity on their own account) and employees; HMRC does not recognise the wider category of "workers". There are certain tax and national insurance benefits from being self-employed so HMRC may dispute how an individual has been categorised. The test applied by HMRC to determine self-employed/employed status is similar to the test applied by the Employment Tribunal when determining employment status for employment protection purposes, but confusingly, neither is determinative of each other. Furthermore, because the UK tax rules do not recognise worker status, an individual can be classed as a "worker" for employment protection purposes but still retain self-employed status for tax purposes.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

In determining if an individual has employee status, the overriding consideration will be the substance of the relationship between the parties. The definition of "employee" and "worker" as set out by statute law are set out below but in short, "employees" work under a contract of employment (also known as a contract of service), whereas "workers" work under a contract to do work personally. However, there is a lack of clarity between the two.

Section 230(1) of the Employment Rights Act 1996 (ERA) defines an employee as follows:

"an individual who has entered into or works under (or, where the employment has ceased, worked under) a contract of employment".

This simple definition is not particularly helpful when it comes to the complex facts of most employer/worker relationships. There are a number of criteria, which have been developed by the courts to determine employment status. The starting point is the test set down in *Ready Mixed Concrete (South East) Ltd v the Minister of Pensions and National Insurance* [1968] 2 QB 467, which determined a four stage test:

i) Mutuality of obligations (that is, the obligation to work and to pay) – a Tribunal would consider whether the individual has the right to a minimum amount of work or pay which would indicate employment status, or whether the individual could refuse work when offered, or could be sent home if a project ended.

ii) Personal service – an unqualified right to substitute another individual would indicate independent contractor status.

iii) Sufficient control by the party for whom the work is being carried out. The tribunal would look at all the facts to determine if the employer had sufficient control over the individual for it to constitute employment status. Factors that the tribunal might consider are:

- the extent to which the individual is subordinate to the employer (for instance, are there appraisals and disciplinary procedures?);
- is the individual integrated into the business (own desk, business cards, email address)?
- does the individual provide his/her own tools and equipment?
- what training and supervision is provided to the individual? Is the individual permitted to take on other work?
- how senior is the individual? The more senior, the less control the employer would be expected to have.

iv) Consistency of the other provisions of the contract with it being a contract of employment. Control will not be enough to determine employment status on its own. Other factors that will be relevant are:

- the extent of the financial risk which is adopted by the individual, such as the risk of making a loss on the contract, termination without compensation, or an obligation to make good any defective workmanship at their own expense;
- whether the individual supplies their services through a service company primarily to limit their liability;
- whether the individual supplies their own insurance cover;
- how much the individual is invested in and manages the business;
- whether the individual is able to profit from their own performance;
- whether the individual is entitled to employee type benefits, paid a salary, or is entitled to holiday or sick pay;
- whether the individual is paid by reference to an annual salary, or a fixed hourly rate or a set fee for the entire job.

The way in which the parties describe themselves will not be decisive as to the individual's employment status. Simply drawing up a consultancy agreement and describing the relationship as a self-employed independent contractor will not necessarily lead to a finding that no employment exists. Nevertheless, the parties' understanding about the nature of their relationship will not be disregarded by the courts, particularly if the situation is marginal.

Worker status

As described in the introduction to this chapter, UK statute law has introduced an additional category of labour, known as a "worker". A worker is defined in section 230(3) ERA

as an individual who has entered into or works under (or, where the employment has ceased, worked under):

"A contract of employment; or

Any other contract, whether express or implied and (if it is express) whether oral or in writing, whereby the individual undertakes to do or perform personally any work or services for another party to the contract whose status is not by virtue of the contract that of a client or customer of any profession or business undertaking carried on by the individual."

Sometimes it is clear that an individual is not an employee, but it may be less clear whether they are either a worker or an independent contractor. As with the test for employment status, the courts have developed a multiple factor test to help determine worker status.

Elements that are required to show worker status can be summarised as follows:

i) Contract – there must be a contract whether oral or in writing, express or implied, between the employer and the individual worker. Unlike employee status, there is no requirement to show an obligation on the employer to provide work and the employee to perform it (mutuality of obligation).

ii) Personal service – it is essential that the individual contracting to do the work agrees to do so themselves, and not by supplying the services of another. Therefore a genuine right to substitute another person will negate any obligation to perform work personally. However, the existence of a contractual term to this effect, which does not reflect the intentions of the parties may be disregarded by a tribunal. This is often because the tribunal will take into account the relative bargaining powers of the parties because companies can often dictate the written terms of any contract, which the individual is bound to accept if they want the work.

iii) Profession or business undertaking exception - the individual will not be a worker if the other party to the contract, for whom the individual is working, is a client or customer of their profession or business undertaking. The tribunal will determine whether the essence of the relationship is that of a worker, or an independent contractor, in business on their own account. For this purpose, the tribunal might consider the dominant purpose of the contract: was it in the employment field, or was it a contract between two business undertakings? There is no test, which is universally applied although the "integration" test is one that is used most commonly. This involves asking:

- does the individual market their services an independent person to the world in general? (This would indicate they are not a worker); or
- was the individual taken on by the employer to work as an integral part of the employer's operations? (this would indicate they are a worker).

In order to establish whether a person is self-employed, the tribunal will assess whether they are "in business on their own account". The factors that should be taken into account include:

- whether the individual provides their own equipment;
- whether they hire helpers;
- the degree of financial risk taken;
- the degree of responsibility for investment and management;
- the opportunity for profiting from sound management.¹

¹ Market Investigations Ltd v Minister of Pensions and Social Security [1969] 2 QB 173

It is also clear that LLP members can be workers. In the leading case of *Clyde & Co v Bates Winkelhof* [2014] UKSC 32, the Supreme Court found that the LLP member was an integral part of the business and the firm was in no sense her client or customer. The court also found that there does not always have to be an element of subordination in the relationship between a worker and their employer, so while the concept of subordination may be helpful in distinguishing between an employee, worker or self-employed contractor, each case needs to be assessed on its facts.

The approach taken by the employment tribunal can be illustrated with the recent claim by Uber drivers that they had worker status. In the highly publicised preliminary hearing in the case of *Mr Y Aslam, Mr J Farrar and Others v Uber* (2015), the Tribunal found that they were indeed workers, some of the factors that the Tribunal took into account included the fact that they found that Uber:

- interviews and recruits drivers;
- controls key passenger information and does not share this with the driver;
- requires drivers to accept trips;
- sets the default route to be taken;
- sets the fare and the driver can only decrease it; the driver is not free to increase it;
- imposes conditions on drivers regarding the type of vehicle they can use, instructs them how to do their work and controls how they perform their work;
- uses rating systems to effectively performance manage/discipline drivers.

These factors indicated that Uber had a level of control over its drivers that was consistent with the drivers being workers for Uber, in that they personally undertook to do or perform work for Uber. The drivers were not acting totally independently and autonomously, as a self-employed contractor would. The tribunal found that the drivers were workers and not independent contractors for so long as the driver had turned on the app, was ready and willing to accept fares and was in the territory in which they were authorised to drive. The tribunal's decision is not binding on other Tribunals but in 2017 it is being appealed to the Employment Appeals Tribunal, which has the ability to create binding precedent.

Meaning of "employment" for discrimination purposes

So far in this section, the discussion has concerned employment status for the purposes of the ERA (which covers matters such as unfair dismissal). A similar definition of worker status is included in other legislation on working time (which includes holiday pay) and national minimum wage. Discrimination rights, however, are treated slightly differently: the Equality Act 2010 (EA 2010) affords protection against discrimination to all persons in "employment" as defined by the EA 2010. There is no distinction made in the EA 2010 between employees and workers, as there is in the Employment Rights Act 1996 (ERA) (see above). "Employment" in the context of the EA 2010 is wider than in the ERA and extends beyond employees, to some persons who would be considered workers under the ERA (as described in the paragraph above "worker status").

The EA 2010 defines "employment" as:

- "employment under a contract of employment, a contract of apprenticeship, or any other contract personally to do work";
- crown employment (including Government Ministers and Civil Servants);
- employment as a member of the House of Commons or House of Lords staff.

Unlike the ERA test for "employee", the EA 2010 test does not specifically exclude those running their own business and working for clients or customers. However, the courts have introduced a similar qualification by a different route. Therefore, for practical purposes, employees and workers will all be entitled to protection from discrimination

under the EA 2010. Certain independent contractors may also be protected but not under the employment provisions of the EA 2010. For example, the EA 2010 provides specific protection against discrimination for police officers, partners, barristers and office holders such as directors. For completeness, it is worth pointing out that volunteers (e.g. to a charity) are not "in employment" and so do not benefit from protection from discrimination under the EA 2010.

Meaning of employee for tax purposes

The tests for employment status are similar in both the employment tribunal and the tax tribunals but despite this, neither test is determinative of the other. This can have confusing results. For instance, the UK tax authority (HMRC) may deem the individual to be an employee for tax purposes, notwithstanding the fact that the individual is not considered an employee for employment law purposes. This may occur where the individual is considered a "worker" for employment law purposes (so is entitled to holiday pay and national minimum wage). In practice, when an individual's employment status has been as determined by an employment tribunal, this might influence their tax status (which will be determined by HMRC or a tax tribunal), but this is not always the case.

b. General Differences in Tax Treatment

There are a number of tax benefits from holding independent contractor status:

- the individual will be responsible for payment of their own tax by self-assessment;
- payment for the individual's services will not be "earnings" for income tax purposes;
- there will be no liability for class 1 National Insurance Contributions (NICs);
- the individual alone is responsible for class 2 NICs and class 4 NICs;
- the individual may need to register for Value Added Tax (VAT) depending on level of turnover.

c. Differences in Benefit Entitlement

Workers are entitled to certain employment rights, including rights to:

- the National Minimum Wage and National Living Wage;
- protection against unlawful deductions from wages;
- statutory paid holiday of 5.6 weeks per year (including public holidays);
- statutory rest breaks including night breaks;
- not work more than 48 hours on average per week or to opt out of this right if they choose;
- protection against unlawful discrimination;
- protection for 'whistleblowing' - reporting wrongdoing in the workplace;
- not be treated less favourably if they work part-time;
- the right to be accompanied to a disciplinary or grievance hearing by a fellow worker or a trade union representative;
- the right not to be subject to a detriment, or offered inducements in relation to trade union membership;
- the right to be automatically enrolled in a pension scheme.

Some workers may also be entitled to:

- statutory sick pay (if their earnings are liable for class 1 National insurance contributions (NICs));
- statutory maternity pay (includes directors whose earnings are taxed in the same way as employees and non-employees who are "employed earners" for NIC purposes, such as agency workers other than models and home workers).

Agency workers have specific rights from the first day at work (see section below for further discussion of agency workers).

All employees are workers. But employees have extra employment rights and responsibilities that do not apply to workers who are not also employees. Rights available to employees include all of the rights workers have (see above) and:

- statutory leave and pay for maternity, paternity, adoption and shared parental leave (note - workers are only entitled to statutory maternity pay);
- rights on dismissal (see section below);
- right to request flexible working;
- right as a fixed term worker not to be treated less favourable than a comparable permanent employee;
- certain rights not to suffer a detriment;
- most rights to time off (including time off for emergencies);
- right not to be refused employment for trade union reasons;
- right to written particulars of employment and itemised pay statement;
- remuneration on suspension on medical grounds;
- right not to be suspended on maternity grounds;
- right of shop and betting employees to refuse Sunday working.

Some of these rights require a minimum length of continuous employment before an employee qualifies for them. For example, an employee requires two years' continuous employment before being entitled to a redundancy payment or to claim unfair dismissal.

Independent contractors who are not workers have very limited statutory rights since the relationship with their client is governed by agreed contractual terms. A self-employed woman may be entitled to claim maternity allowance but all the other benefits relating to employees and workers described above will not be relevant.

d. Differences in Protection from Termination

Employees benefit from a range of statutory protections from dismissal including, for example:

- statutory minimum periods of notice;
- written statement of reasons for dismissal;
- right not be unfairly dismissed;
- statutory redundancy payment;
- rights on employer's insolvency and to benefit from the state guarantee fund.

Workers, on the other hand, do not benefit from any of the above protections on termination. However, there are some indirect protections available through statute on termination of a worker's contract:

- for a discriminatory reason (such as a reason relating to sex, race, sexual orientation, religion or belief, age); or
- by reason of having made a protected disclosure (whistleblowing).

e. Local Limitations on Use of Independent Contractors

The main limitation on the use of independent contractors in the UK is the risk that they will be re-classified as employees or workers. See below for more information on this risk.

f. Other Ramifications of Classification

Implied duty of mutual trust and confidence

Under the common law, there is an implied duty of mutual trust and confidence in all employment contracts. This term was developed and reformulated but was finally confirmed in the case of *Malik and another v Bank Of Credit & Commerce International SA* (in compulsory liquidation) [1998] AC 20 as follows:

"The employer must not, without reasonable and proper cause, conduct itself in a manner calculated and likely to destroy or seriously damage the relationship of trust and confidence between employer and employee."

The obligation ensures that both parties are protected from acts that are not prohibited by statute or the contract of employment e.g. an obligation on the employer to protect the employee from being bullied by other employees. There is no implied duty of mutual trust and confidence found in contracts for services, therefore independent contractors and their clients are not subject to this duty.

Vicarious liability

Companies will generally be liable for the acts done by employees or workers in the course of employment. The general rule for independent contractors is that clients will not be liable for negligent or tortious acts committed by an independent contractor in the execution of the work for which they were engaged.

However, clients may be liable for any loss suffered as a result of a breach of a "non-delegable duty" by an independent contractor. These "non-delegable duties" may arise either under statute or at common law. To avoid liability the client must show that it engaged a reasonably competent individual to perform the work and ensured that the individual adhered to a reasonable standard of care.

g. Leased or Seconded Employees (including Agency Workers)

Businesses, which need staff on a short term basis, perhaps to deal with an increase in workload or for a one-off project, might consider using agency workers. The agency worker will obtain work from, and is paid by an agency, known as an "employment business" (defined by the Employment Agencies Act 1973 as 'the business of supplying people in the employment of the person carrying on the business, to act for, under the control of other people in any capacity') and is not directly employed by the client. Seconded employees operate within a similar tripartite arrangement in circumstances where the employee is assigned, by their original employer, to a third party on a temporary basis. See further below.

The agency will usually have numerous agency workers on its books, and each agency worker may be registered with a number of agencies in order to have the best chance of obtaining work. The agency worker is not under an obligation to accept work when offered, but once accepted they will be bound by the terms of the particular assignment. The end user will pay the agency for the work done and the agency will, in return, pay the agency worker.

The agency will have an agreement with the client, and a separate agreement with the agency workers, but there will not usually be an agreement between the agency worker and the client. In light of this three-party arrangement, the agency worker is likely to be classed as a worker and not an employee. However, occasionally the employment status of an agency worker may not be clear, so the rights they are afforded will depend upon whether they are considered to be an employee or worker. The agency worker might therefore seek to establish that they are an employee of the agency or of the client

(although they cannot be both). Sometimes the contract between the agency and the agency worker is explicitly a contract of employment and in those circumstances the chances of there being an implied contract of employment between the agency worker and the client are small.

The employment status of the agency worker will depend on the circumstances and the existence of the elements outlined above in the *Ready Mixed Concrete* case. The tribunal will be looking for the existence of a contract of service with either the agency or the client. This is to establish whether an agency worker is either party's employee or worker. The difficulty in defining a contract of service in these particular arrangements is mainly due to the roles exercised by both the agency and client which are normally executed by one employer.

Where an agency worker has worked for an end user for a long period of time, there is an increased risk that they will claim that there is an implied contract of employment between them and the client. The tribunal will look at the reality of the situation, to ascertain who actually exercises sufficient control over the worker. Whilst the tribunal will not assume one way or the other, a contract should only be implied where "necessary" to explain the work undertaken by the worker for the end user. Usually, a contract of service will not be implied since in most cases the client will not specify any preference as to which worker is supplied to them so it will be difficult to establish that there is any obligation on the client to provide work to that particular agency worker, or for that worker to accept work. However, the tribunal will consider whether the parties have changed their behaviour since the start of the relationship. Factors that will be relevant include the client's day to day control, such as whether the agency worker has been disciplined under the disciplinary procedures of the end user, or whether the end user has acted as though the worker was a fully integrated member of staff.

Aside from the rights granted to agency workers based on their employment status, agency workers have various additional statutory protections. A key protection (under the [Agency Workers Regulations], which are the UK implementation of the [Agency Workers Directive] is the right to the same pay and basic working conditions as permanent staff after a 12-week qualifying period. Other rights include:

- protection from discrimination;
- right to receive the national minimum wage;
- right to statutory sick pay if they satisfy the definition of an 'employed earner' for national insurance contributions purposes; and
- rights to statutory maternity, paternity, adoption or shared parental pay from the agency if they are considered to be an 'employed earner' for national insurance contributions purposes and if further conditions are met.

A seconded employee is an employee that is assigned to work for a different part of their organisation or for another organisation (the assignment can therefore be internal or external) and is for a temporary basis. The terms of the secondment will be set out in a secondment agreement, which will outline the relationship between the original employer and the third party host that the employee is assigned to.

The general view is that the first organisation, the employee's original employer, will remain their employer throughout the secondment. It may be said that the services provided by the employee have simply been transferred to the third party host temporarily. However, occasionally an employment relationship may be established between the seconded employee and the third party host if the requisite level of control, mutual obligation and personal performance elements from the *Ready Mixed Concrete* case mentioned above are present.

The employment status of a seconded employee is important because it will impact upon the rights and the protections they are afforded as an employee or a worker. A finding that the seconded employee is the third party host's worker or employee will give rise to the seconded employee having statutory rights against the third party host (see list of employee/worker rights above). An employee on secondment to the UK may in any event be able to bring UK claims against his/her non-UK employer.

h. Regulations of the Different Categories of Contracts

There are also 'casual workers' who may be engaged in a variety of ways, such as on a part time or fixed term contract, or a 'zero hour' contract under which the employer is under no obligation to provide a minimum amount of work but the individual is generally obliged to be available to work when asked. There are also 'homeworkers', who may work exclusively at home on a full-time or part-time basis.

The test to determine the employment status of these individuals is exactly the same as for any other individual. If the factors that establish an employee or worker are found in the relationship then they will be recognised as such. As explained above, one particular factor, mutuality of obligation, is key in determining employment status. Casual work often involves individuals being engaged sporadically so that there is insufficient mutuality of obligation for the casual worker to be recognised as an employee or worker. However, in *St Ives Plymouth Ltd v Haggerty* UKEAT/0107/08, the court found that there was sufficient mutuality of obligation in the gaps when no work was performed to infer the existence of an 'umbrella contract'. If the individual can show that there is an 'umbrella' contract of employment which continues to exist during periods when he or she is not working, then it is likely that they will be considered an employee or worker, subject to meeting the other parts of the tests.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

It is essential that the parties clearly define their relationship in writing to establish the individual's status – whether that be the status of an employee, worker or self-employed contractor/consultant. The written terms will usually determine the true legal relationship between the parties. Nevertheless, if it is alleged that the written terms do not reflect the reality of the relationship, the tribunals will investigate allegations that the written terms are not representative of the actual terms agreed, and will determine the actual nature of the relationship between the parties.

The tribunal will examine evidence of how the parties conducted themselves and what their expectations of each other were. The tribunal will ignore express contractual terms, which are inconsistent with the reality of the relationship between the parties. Furthermore, it does not matter that the parties did not intend to misrepresent the true nature of their relationship if it transpires that certain contractual terms were a sham. For example, in the leading case of *Autoclenz v Belcher and others* [2011] UKSC 41, workers who provided car valeting services under contract for a single client all signed agreements which expressly said they could provide substitutes and could refuse work. On the face of it, these clauses indicated self-employment, but evidence showed that these clauses were never invoked. The tribunal examined the evidence and found that the actual legal obligations of the parties should be determined from all the evidence including the parties' conduct and any written terms, and found that the individuals were in fact employees.

In practice, as mentioned above, an individual's employment status can influence their tax status. However, as self-employment comes with considerable tax benefits to the individual, an individual's decision as to whether to bring a claim for employment status in an employment tribunal should be considered carefully in light of this risk.

b. The Legal Consequences of a Re-Characterisation

Employment rights

As mentioned above, companies are only obliged to provide the majority of statutory protections and benefits to those who they employ as employees and workers. However, where an individual is engaged as an independent contractor, but in reality the true legal relationship is more akin to employment, the individual will actually be entitled to all the statutory protections and benefits that normally accrue to an employee or worker (as appropriate). In some cases, the employee will seek to backdate their claim to cover the period over which the employment relationship is deemed to have existed.

A particularly thorny issue in these cases concerns accrued holidays. An independent contractor successfully claiming worker status will be entitled to paid holidays going forward and may be entitled to take some accrued holiday. Workers are entitled to a minimum of 5.6 weeks' paid holiday per year (pro-rated for part time workers). As a general rule, untaken holiday cannot be carried forward to the next holiday year, except where the worker is "unable or unwilling" to take holiday because they are on sick leave, and, as a consequence, do not exercise their right to annual leave. The recent case of *The Sash Window Workshop (1) Dollar (2) v King [2014] UKEAT 0057_14_0112* considered this point in relation to a worker who had been wrongly classified as an independent contractor. The Employment Appeal Tribunal (EAT) decided that if a worker is prevented from taking annual leave during a leave year for any reason beyond their control, i.e. not just because of long-term sick leave, then arguably that annual leave can be carried forward to the next leave year and is not lost. This point was referred to the Court of Justice of the European Union (ECJ) in April 2016 and is currently awaiting a hearing date.

Where the worker's contract or employment has ended and there is accrued holiday outstanding, the worker may be able to make a claim under the Working Time Regulations 1998 for a payment in lieu of accrued unused holiday for the holiday year in which the contract ends. The worker may also be entitled to payment for accrued leave carried over from earlier leave years, although for workers who had been wrongly classified as independent contractors the position is not entirely clear and is awaiting consideration by the ECJ in *Sash Windows* (see above). A claim must be brought within three months of termination of the worker's contract or employment, and there is a two year limit on the amount of back pay that can be claimed in most cases.

Tax

If an individual is deemed by HMRC (or a tax tribunal) to be an employee for tax purposes, it will have the following consequences –

- the individual's fees will be subject to income tax as "earnings";
- the fees will be subject to class 1 National Insurance Contributions (NICs):
 - primary class 1 NICs will be due from the individual;
 - secondary class 1 NICs will be due from the employer;
- the employer must deduct tax and NICs at source from the individual's earnings under the system known as Pay As You Earn (PAYE).

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The remedy available to persons seeking employee status will depend on the rights and benefits sought. Most commonly, a so-called independent contractor might seek em-

ployment status when faced with termination of their contract by their "client". A claim for unfair dismissal and/or a redundancy payment in the employment tribunal will be the most usual form of claim. Another common type of claim in the employment tribunal is for holiday pay and national minimum wage. Given the rights available to both employees and workers, the tribunals have seen claims by large groups of casual workers such as so-called zero hours workers, and other individuals such as drivers and couriers working in the Gig economy, who have been characterised as independent contractors but who consider themselves "workers" (see below).

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Employment rights

Where the individual's contract has been terminated and the tribunal determines them to be an employee, the usual remedy will be an award of compensation against the employer in the form of a basic award for unfair dismissal or a statutory redundancy payment. Both these awards are calculated in the same way and are dependent on weekly pay, age and length of service (maximum £14,370 from 6 April 2016). For unfair dismissal claims, there is also commonly a compensatory award (maximum £78,962 from 6 April 2016). Less common remedies for unfair dismissal include reinstatement or re-engagement, and, in very limited circumstances, an additional award. Where the contract has been re-characterised to "**worker status**", the individual may have a range of claims such as: accrued holidays or, if the worker's contract is terminated, accrued holiday pay (see 3.2 above), back pay where the worker has not received National Minimum Wage, and compensation for breach of working time rules (such as failure to give appropriate rest breaks).

Pensions

The Pensions Regulator is charged with ensuring employers comply with legislation requiring employers to automatically enrol "job holders" into pension schemes. The definition of jobholder in the pensions legislation is the same as the definition of "worker" used in the employment legislation such as the Employment Rights Act 1996 (see paragraph 2.1 above). Where a self-employed contractor is re-characterised as a worker or a job holder, it could find itself facing substantial back payments of pensions contributions, including interest payments.

Tax

If HMRC or a tax tribunal deems an individual to be an employee for tax purpose and there is any underpayment of tax, HMRC will pursue the employer in the first instance for under-deducted tax, employer's NICs and also any penalties owing and interest accrued on the sums.

The employer may seek a direction from HMRC that:

- limits the employer's liability to the amount outstanding if some or all of the tax in question has been paid by the employee;
- the employee should pay the unpaid tax. This will only succeed if HMRC is satisfied that:
 - the employer took reasonable care and the failure to deduct was made in good faith, or
 - the employee knew that the employer "willfully failed" to deduct tax.

In more limited circumstances, the unpaid employer's NICs can be recovered directly from the employee. This will apply where the failure to deduct NICs is due to an act or default of the employee and not to any negligence on the part of the employer or the employee knew that the employer "willfully failed" to deduct employee NICs and has

not recovered them from the employee. In practice, this requirement is rarely met so recovery of NICs is almost always from the employer.

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTOR RELATIONSHIP

a. How to Properly Document the Relationship

Framing the relationship between the client and an independent contractor should be approached with caution, as careful wording is needed to ensure that the contract does not reflect an employment relationship.

Primarily, the wording should reflect the flexibility and reality of the self-employed nature of the relationship. Critically though, the parties must ensure that the contract is an accurate reflection of the actual terms agreed between the parties. If it is not and the employment status is challenged, the tribunal will look behind the terms and consider all the circumstances to determine if they are a genuine reflection of the reality of the arrangements. This will be the case even if the contract contains an "entire agreement" clause. Other points to note are as follows:

- the label given to the contract will be important but not conclusive since the issue will be determined objectively;
- the wording should confirm that nothing in the contract prevents the independent contractor from being engaged, concerned or having any financial interest in any other business. To the extent possible, post-termination restrictive covenants such as non-competition and non-solicitation clauses (which are often associated with employee status) should also be avoided;
- it will be helpful to include a clause which properly defines the independent contractor's services;
- a clause, which entitles the independent contractor to send a substitute in their place to continue to provide the services under the contract, is a useful clause which may indicate self-employed status.

b. Day-to-Day Management of the Relationship

Recent case law has made it clear that the everyday reality of the relationship between client and independent contractor should accurately reflect the self-employed status. The presence of any of the elements set by the Ready-Mixture Concrete case (see section 2.1 above) would suggest that there is an employment relationship in place instead and care should be taken to ensure that this is avoided. Substantive factors include:

- whether the independent contractor has the right to decide the price of their services;
- whether the independent contractor can promote, develop and continue to provide services of their accord;
- how fully integrated the independent contractor is in the client's business and workplace;
- whether the independent contractor is expected to provide his own tools and equipment.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Much has been written recently about the so-called "gig economy" (also known as the

sharing or platform economy). As of the start of 2017, a number of official inquiries are underway looking into the implications of the gig economy. Starting in October 2016, the Business, Energy and Industrial Strategy (BEIS) Committee launched an inquiry into the future of the world at work, focusing on the rapidly changing nature of work, the status and rights of agency workers, the self-employed, and those working in the gig economy.² In November 2016 BEIS launched the Independent Review of Employment Practices in the Modern Economy, to be led by Matthew Taylor. The review will consider the implications of new models of working on the rights and responsibilities of workers, as well as on employer freedoms and obligations. The review is expected to last six months and will report in summer 2017 and the outcome will inform the government's industrial strategy. Further inquiries, both launched in December 2016, include the inquiry by the Work and Pensions Committee into the implications on the welfare system including state pensions, and the inquiry into the tax issues of the gig economy by the Office of Tax Simplification.

Preceding these inquiries was an inquiry into the working practices at Sports Direct and the BEIS Committee's inquiry on the Digital Economy, which recommended that workers using the platforms have reasonable employment conditions and are not vulnerable to exploitation. Also relevant are the recent news stories and cases concerning the status of individuals working for Uber, Citysprint and Deliveroo. News stories about exploitation of workers, including failure to pay the national minimum wage, failure to give adequate work breaks, poor working conditions, and generally lack of job security, have raised questions about employment status and lack of worker rights.

This is not the first time that employment status has been considered by the UK government. In 2014, the coalition government launched a review to improve clarity and status of the British workforce. Spurred by the disquiet over exploitation of zero hours and agency workers, the Government sought a better understanding of the issues in order to consider a potential extension of employment rights to certain groups of workers, and great clarity and transparency in employment law so that there is less confusion about what rights an individual is entitled to. After a change of government in 2015, the review made no further progress.

The Advisory, Conciliation and Arbitration Service (ACAS) will be looking at gig work in more depth in 2017 and is expected to issue further guidance around the many different types of employment status and accompanying workplace rights later in 2017.

b. Recent Amendments to the Law

As mentioned earlier, in 2016 and early 2017 there have been a number of claims by individuals employed in the "gig economy" such as drivers who work for Uber, and couriers working for Deliveroo and Citysprint. The highly publicised preliminary hearing in the case of *Mr Y Aslam, Mr J Farrar and Others v Uber (2015)* made the headlines when the tribunal held that the claimants, who were drivers that contracted with Uber, were 'workers.' Soon after that decision, the Court of Appeal³ decided that a so-called self-employed plumber working exclusively for Pimlico Plumbers for nearly six years was also a worker and so was entitled to basic workers' rights, despite being self-employed for income tax purposes (and was VAT registered).

The reasoning in these decisions highlight the current approach in deciding employment status; making it clear that the reality of the arrangements between the business, the individual and the customer will be closely scrutinised, and contracts will be disregarded if these do not reflect the reality of the arrangements. As already stated, the tribunal's

² The inquiry's terms of reference extend to considering whether the term "worker" is sufficiently defined, and how, in particular, agency workers, casual workers and the self-employed (including those working in the "gig economy") should be categorised for the purposes of tax, benefits and employment law.

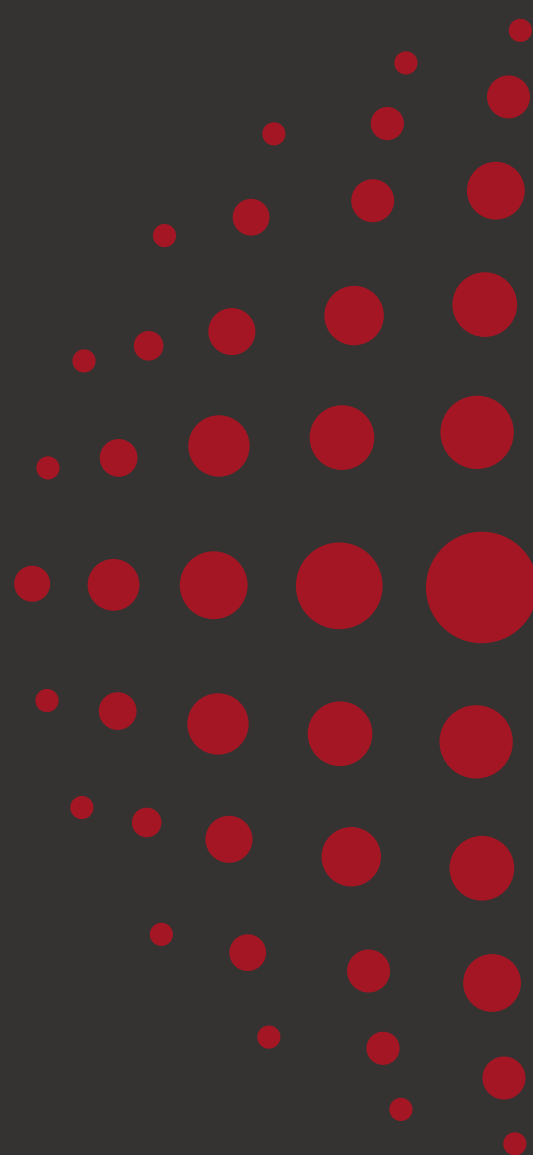
³ *Pimlico Plumbers Ltd and anor v Smith* [2017] EWCA Civ 51

decision in the Uber case is not binding on other tribunals but in 2017 it is being appealed to the EAT. It is likely that the Pimlico plumber case will be appealed to the Supreme Court. Employers and employment lawyers will be watching this, and other "gig-economy" worker status cases with interest.

VI. CONCLUSION

Employers who require a supply of flexible labour may engage agency workers, casual workers and, frequently, independent contractors. For the individual, there are certainly tax advantages in being an independent contractor rather than an employee. The UK government is keen to ensure business retains this flexibility to remain competitive, but is also concerned that individuals' rights are protected from abuse from unscrupulous employers. The courts have demonstrated a willingness to preserve this balance by looking behind the company-drafted documentation, which purports to preserve self-employed status, to the practical reality of the situation (which might indicate otherwise). The lure of better rights set against the lack of job security for independent contractors sometimes means that an independent contractor will challenge their employment status in the employment tribunal, even if this might risk their self-employed tax status. We have seen in this chapter that there are a number of criteria, which have been developed by the courts to determine employment status and although recent case law has emphasised the importance of looking at the reality of the relationship, it still remains of the utmost importance that the relationship is properly documented. This will not be decisive in determining status, but it can tip the balance if the situation is marginal.

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UNITED STATES OF AMERICA

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I. OVERVIEW

a. Introduction

The past decade, particularly during the years of the Obama Administration, has seen an increased administrative focus on potential independent contractor misclassification by the U.S. Department of Labor (“DOL”) and the Internal Revenue Services (“IRS”). Independent contractor misclassification is a nationwide issue, spanning all industries – both on-demand and more traditional business models, and all regions. Commonly cited industries include: transportation, ride sharing, janitorial, food services, IT services, courier services, day care, commercial cleaning, and startups. The DOL estimates that approximately 3.4 million workers in the U.S. are misclassified as independent contractors resulting in a lack of employee entitled benefits and protections, as well as an approximate 3.4 billion U.S. treasury revenue loss in Income Tax, Social Security, Medicare, and unemployment insurance trust fund contributions.

Employer risks resulting from independent contractor misclassification include:

i. Liability for unpaid employment taxes

- past federal payroll taxes (3 years back, or more)
- state payroll taxes
- up to 100% penalty—if willful failure
- income tax not withheld
- trust fund recovery penalty for responsible persons

ii. Failure to pay minimum wage and overtime

- recovery by administrative authorities or civil litigants of unpaid minimum wage/overtime
- liquidated damages (100 % percent penalty)
- application of damage model to all workers in same job, not just individual worker
 - i.e. liquidated damages paid to all workers in the position misclassified as independent contractor.
- DOL supervision over payment of wages
- attorneys’ fees and cost

iii. Unfair labor practices liability under the National Labor Relations Act

iv. Immigration liability to the extent employers hire non-U.S. citizen workers as independent contractors to avoid verification of their citizenship status or obtaining of proper work visas.

v. Exposure to claims for coverage under employee benefit plans (Note: No statute of limitations)

The distinction between employees and independent contractors is defined somewhat differently depending on the statutory context. Key legislation relating to independent contractor misclassification includes:

- IRS: U.S. Tax Code (federal income tax withholding)
- U.S. Department of Labor:
 - FLSA (Fair Labor Standards Act – minimum wage and overtime);
 - FMLA (Family and Medical Leave Act);
 - ERISA (Employee Retirement Income Security Act)
- State Unemployment Laws/Agencies

- State Workers' Compensation Laws/Agencies
- State Income Tax Withholding
- Federal Anti-Discrimination Laws (Title VII, ADA, etc.)
- State and Local Anti-Discrimination Laws
- NLRA (National Labor Relations Act)
- IRCA (Immigration Reform and Control Act)

In September 2011 the DOL announced its "Misclassification Initiative"¹ – a program designed to establish joint/coordinated efforts between the DOL and the states. Since 2011, 35 states have signed a Memorandum of Understanding with the DOL and have passed bipartisan legislation to limit independent contractor misclassification. This form of state legislation typically includes: increased penalties for independent contractor misclassification, more stringent independent contractor status testing, and establishment of a state task force to address independent contractor issues. As a result of this joint initiative between the DOL and the state legislatures, in 2015, DOL investigations resulted in \$74 million in back wages for more than 102,000 workers. It should be noted that during this same period there has been no new federal legislation addressing independent contractor misclassification.

With the transition to a new Presidency and new leadership in US administrative agencies in 2017, it is possible that a more pro-employer direction will ultimately take hold in interpretation of the relevant statutes and regulations.

II. LEGAL FRAMEWORK DIFFERENTIATING EMPLOYEES FROM INDEPENDENT CONTRACTORS

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

As mentioned above, there is no uniform definition of "employee" under the laws of the United States, and no single standard or test exists to determine conclusively whether a worker should properly be classified as an independent contractor or employee. Classification issues may and frequently do arise in the U.S. under an intricate patchwork of federal and state laws and legal principles relating to taxation, employee benefits, employee wages and work hours, collective bargaining, workplace safety and health, employment discrimination and other employment-related matters. As discussed below, courts and government agencies have developed different and often divergent classification standards. The outcome of any classification analysis, therefore, is highly context-dependent.

Navigating the manifold standards and expectations under federal and state laws in the day-to-day implementation of an independent contractor arrangement can be a challenging task and the risk of misclassification is by no means insignificant. Enforcement efforts by government agencies have been stepped up markedly in recent years, while private collective and class action lawsuits abound. Any independent contractor relationship should be carefully reviewed and managed to avoid the potentially serious consequences of an adverse agency ruling or court judgment.

The Common-Law Test

The United States Supreme Court has held that when a statute does not adequately define "employee," the term must be interpreted by reference to the common law of agency.² The common-law test has been applied in a variety of contexts. Such contexts include claims by allegedly misclassified employees seeking participation in employer-provided welfare or retirement benefit plans under the federal Employee Retirement

Security Act ("ERISA");³ claims to determine collective bargaining rights under the National Labor Relations Act ("NLRA");⁴ claims to decide whether a company is required to withhold from compensation for state unemployment compensation benefits;⁵ and various other statutory and common-law claims.⁶

The central question to be answered under the common-law test is whether the hiring party retains the right to control the manner and means by which the work is to be accomplished. This means that courts must focus their inquiry on whether the hiring party "has the right to control and direct the work, not only as to the result to be accomplished by the work, but also as to the manner and means by which that result is accomplished."⁷ When the hiring party retains the right to control the manner and means by which the work is to be accomplished, the worker is considered an employee – even if the hiring party actually never exercises the right.⁸

Although the extent to which the hiring party actually supervises the "means and manner" of the worker's performance is a core factor under the common-law misclassification test, it is far from the only one. Among the numerous additional factors courts must weigh as part of their overall analysis are the following:

- the skill required;
- the source of the instrumentalities and tools;
- the location of the work;
- the duration of the relationship between the parties;
- whether the hiring party has the right to assign additional projects to the hired party;
- the extent of the hired party's discretion over when and how long to work;
- the method of payment;
- the hired party's role in hiring and paying assistants;
- whether the work is part of the regular business of the hiring party;
- whether the hiring party is in business;
- the provision of employee benefits; and
- the tax treatment of the hired party.⁹

The common-law test requires a careful balancing of all relevant factors. No one factor controls the outcome. The weight given to each may vary from case to case depending on the particular facts and circumstances. In no case, however, will the terms of any written agreement between the company and the worker by themselves prove dispositive of the outcome.

A recent federal district court decision illustrates the common-law approach. In this decision¹⁰, the court refused to dismiss a class action lawsuit filed by insurance agents they were employees under the common-law test and therefore entitled to certain employee benefits under ERISA. The court denied the company's motion to dismiss the case, finding that a series of factors could be interpreted to indicate employee status. These factors included the insurance company's requirement that agents sell company products exclusively and only use company-owned hardware and software; the

¹ Wage and Hour Division, *Misclassification of Employees as Independent Contractors*, DOL, available at <https://www.dol.gov/whd/workers/misclassification/>.

² See *Nationwide Mutual Insurance Co. v. Darden*, 503 U.S. 318, 322-24 (1992).

³ Employee Retirement Security Act of 1967, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended at 29 United States Code ("U.S.C.") §§ 1001–1461 (2006) and in scattered sections of the Internal Revenue Code).

⁴ National Labor Relations Act of 1935, 29 U.S.C. §§ 151–169.

⁵ See, e.g., *Cantor v. Cochran*, 184 So. 2d 173 (Fla. 1966); *Leone v. United States of America*, 910 F.2d 46 (2d Cir. 1990), cert. denied, 499 U.S. 905 (1991) (applying New York law).

⁶ For example, variants of the common-law test have been used by courts and government agencies to determine whether a worker is entitled to protection under federal and state laws prohibiting workplace discrimination and retaliation.

⁷ *N.L.R.B. v. Steinberg*, 182 F.2d 850, 857 (5th Cir. 1950).

⁸ *N.L.R.B. v. Associated Diamond Cabs, Inc.*, 702 F.2d 912 (11th Cir. 1983).

⁹ *Darden*, 503 U.S. at 323-24.

¹⁰ Case No.1:13 CV 437 (N.D. Ohio Aug. 9, 2013) : *Jamal v. American Family Insurance*.

company's ability to fire the agents at any time with or without cause; the company's right to determine where agents' offices were located and what their office hours would be; and the company's actual monitoring of agents' daily work and compliance with production and conduct requirements.

The IRS Right to Control Test

Perhaps the most commonly used test is a variant of the common-law test developed by the U.S. Treasury Department's Internal Revenue Service ("IRS") to determine whether a worker should be deemed an employee for income tax purposes. The IRS has historically applied a lengthy 20-factor test.¹¹ In recent years, however, the agency restructured its approach and now applies a simplified "Right to Control Test," which groups 11 factors into three broad categories.¹² As with the common-law test, the critical inquiry focuses on the degree to which the business retains the right to control the manner and means by which the work is performed.

The Right to Control Test can be summarized as follows:

A) Behavioral control. Behavioral control refers to the degree to which the company retains the right to direct and control how the worker performs the task for which the worker is hired. Whether or not the business in fact exercises that right is irrelevant.¹³ The focus is simply on whether the company has reserved the right of control to itself. There are two behavioral control factors:

- does the business provide instructions to the individual regarding (a) when and where to perform work, (b) what tools or equipment should be used, (c) where supplies and services should be purchased, (d) whether and what assistants the worker may hire, (e) whether the work must be performed by a specified individual, and (f) in what order or sequence the work must be completed?
- does the business provide training to the worker?

Independent contractors normally use their own methods to perform work and require little to no training. Positive answers to the above questions therefore point to the existence of an employment relationship.

B) Financial control. Financial control factors are intended to capture the degree to which the business has the right to control the business aspects of the job:

- does the business pay the worker's business expenses? Routine reimbursement of a worker's business expenses can be indicative of an employment relationship.
- has the worker made a significant investment in the services performed? Typically, independent contractors, but not employees, have invested substantially in the work, for example by maintaining an office or other facilities where services are performed.
- does the worker make his or her services available to the general public? Independent contractors generally remain free to advertise their services and are available to work in the relevant market.
- is the worker paid a flat fee, or by the hour, week or month? Employees commonly receive a regular wage based on a certain time interval, whereas payment on a flat fee, per-job basis suggests independent contractor status.
- does the worker have the opportunity to realize a profit or loss from the work? This is ordinarily a hallmark of independent contractor status.

¹¹ See IRS Worker Classification Training Manual (March 4, 1997); IRS Publication 15A (2013 edition).

¹² See IRS Worker Classification Training Manual (March 4, 1997); IRS Publication 15A (2013 edition).

¹³ See *Gierek v. Comm'r*, 66 T.C.M. (CCH) 1866, 1868-69 (1993) (when a company has a right to control the worker, the worker may be considered an employee, even if the company did not actually exercise control).

C) Type of relationship. As the nature of the relationship between the business and the worker can provide further evidence of control, the IRS also examines the following additional factors:

- does the worker have an opportunity to participate in certain employee welfare and pension benefits, such as health insurance, a pension plan, vacation pay, or sick pay? Benefits typically are provided only to employees.
- how permanent is the relationship? An independent contractor relationship is ordinarily of limited duration and defined by the length of the specific project for which the contractor is hired. Hiring a worker on an indefinite basis indicates intent to create an employer-employee relationship.
- are the worker's services a key aspect of the company's regular business? If so, an employment relationship is more likely to exist.
- do the terms of a written contract between the business and the worker show that the parties intended to create an independent contractor relationship? This factor is normally the least important, because courts must examine first and foremost the parties' actual practice.

The Economic Realities Test

Neither the common-law test nor its IRS variant governs where federal wage-and-hour laws are concerned. In the United States, federal minimum wage and overtime pay standards are established by the Fair Labor Standards Act ("FLSA").¹⁴ Recognizing that the FLSA was enacted to remedy low wages and long working hours, the United States Supreme Court has long held that the common-law distinctions between employees and independent contractors do not apply when determining FLSA coverage.¹⁵

Instead, courts must decide whether a worker has been properly classified as a matter of "economic reality."¹⁶ The key question to be answered under the Economic Realities Test is this: Is the worker economically dependent on the hiring party, or is the worker truly in business for him- or herself? If economic dependence is found, the worker will be classified as an employee, even if the employer does not exercise full control of the means and manner of the worker's performance.

Resolution of this question requires a balancing of the following factors in light of the totality of the circumstances:

- the degree of control the business exerts over the worker;
- the worker's opportunity for profit or loss;
- the worker's investment in the business;
- the permanence of the working relationship;
- the degree of skill required to perform the work; and
- whether the services are an integral part of the company's business.¹⁷

Various additional factors may also be considered as part of the economic realities test, such as whether the business has the power to hire and fire employees, supervises and controls employee work schedules or conditions of employment, determines the rate and method of payment, and maintains employment records. No one factor is determinative.¹⁸ All must be carefully weighed and take account of the factual circumstances of each particular case.

¹⁴ Fair Labor Standards Act of 1938, as amended, 29 United States Code §§ 201 et seq.

¹⁵ See *Goldberg v. Whitaker House Coop.*, 366 U.S. 28, 33 (1961).

¹⁶ The Economic Realities Test is used not only to resolve independent contractor/employee issues under the FLSA but also to determine whether a business must make employer tax contributions on behalf of an individual to the U.S. Social Security system, which provides certain retirement and disability benefits. See *United States v. Silk*, 331 U.S. 704, 713 (1947).

¹⁷ See, e.g., *Barlow v. CR England, Inc.*, 703 F.3d 497, 506 (10th Cir. 2012); *Brock v. Mr. W Fireworks, Inc.*, 814 F.2d 1042 (5th Cir. 1987).

¹⁸ See *Rutherford Food Corp. v. McComb*, 331 U.S. 722, 730 (1947).

The ABC Tests

Many U.S. states have wage-and-hour laws that provide additional or greater protections beyond those set out in the FLSA. These states employ any one of a number of different tests to determine whether misclassification issues exist. The “ABC Test” represents one of the more commonly used alternatives not only to determine exempt status under state wage-and-hour laws but also to evaluate whether a worker should be deemed an employee for state unemployment tax purposes.

Although applications of the ABC Test are not uniform, it generally places the burden of establishing independent contractor status squarely on the hiring party. In its broadest form, the ABC Test provides that a worker should be considered an employee unless the business can establish that:

- the worker has been, and will continue to be, free from control or direction over the performance of the work under both the terms of the contract and in fact;
- the services are either provided outside the usual course of the business or performed outside of all the places of business of the enterprise; and
- the worker is customarily engaged in an independently established trade, occupation, profession, or business.

In most, but not all, states, all three conditions must be met. As a result, meeting independent contractor requirements can be particularly onerous where the ABC Test applies.

As the above reflects, courts and legislatures in the United States have woven a complex tapestry of legal standards for determining independent contractor status. Further complicating the analysis, employee status may also need to be determined under laws governing workers’ compensation insurance for individuals who suffer work-related injuries or illness; laws protecting whistleblowers or prohibiting discrimination in employment; and various other employment-related statutes. Depending on the statute, state agencies and courts may use variants of the common-law, IRS, economic-realities and ABC tests discussed above.

Not surprisingly, application of the many different tests for determining employment status can lead to diverging results. An individual may, for example, be classified as an independent contractor for state or federal income tax purposes, yet is deemed an employee for purposes of workers’ compensation law and be qualified for such benefits. Businesses should remain mindful of the fact that each situation must be evaluated on its own merits.

Summary of Tests Used Under Key Federal Statutes

Certain Federal Laws explicitly require that a particular test be used to determine the status of a worker as an employee or independent contractor. Below is a list of which test applies to which statute.

Common Law Test

- Federal income taxes, Medicare taxes, Social Security taxes, Federal unemployment taxes
- National Labor Relations Act (NLRA)
- Employee Retirement Income Security Act of 1974 (ERISA)
- Immigration Reform and Control Act of 1986 (IRCA)
- Americans with Disabilities Act (ADA)
- Copyright laws

Economic Realities Test

- Fair Labor Standards Act of 1938 (FLSA)
- Title VII of the Civil Rights Act of 1964 (Title VII)
- Age Discrimination in Employment Act of 1967 (ADEA)
- Family and Medical Leave Act (FMLA)
- Migrant and Seasonal Agricultural Worker Protection Act

b. General Differences in Tax Treatment

There are significant tax advantages for businesses when workers are classified as independent contractors. U.S. employers must pay one-half of an employee’s required social welfare taxes for government-provided Social Security retirement and medical benefits (known as “Medicare”). Typically, these equal approximately 7.65 percent of an employee’s wages. Independent contractors, by contrast, must pay the full amount without any contribution from the hiring business. Employers must also withhold state and federal employee income taxes from an employee’s paycheck, whereas independent contractors pay these taxes on their own in the form of a self-employment tax. Finally, the amount of an employer’s contributions to federal and state unemployment insurance funds depends on the size of the employer’s workforce, but does not take into account independent contractors.

From the perspective of the individual as well, substantial financial benefits can be reaped from holding independent contractor status. Independent contractors need only make quarterly tax contributions and can thus realize benefits from the greater control the absence of mandatory withholdings from each paycheck can afford. Social welfare benefits, in turn, need to be paid only once a year and one-half of the contribution can be deducted from the individual’s income tax. Moreover, unlike employees, independent contractors are able to deduct a wide range of direct and indirect business-related expenses from their taxable income. The increased flexibility and potential for greater actual earnings therefore render independent contractor status an attractive option for many workers.

That said, the adverse tax consequences flowing from misclassification of employees as independent contractors, can be a matter of significant concern, particularly when large groups of similarly-situated workers are found to be similarly misclassified. Recent years have seen an increasing focus on aggressive enforcement actions on the part of not only the Department of the Treasury, but also other federal and state agencies. As a result of new information-sharing agreements between agencies, a finding by the IRS that a business has misclassified employees may now lead to audits and further enforcement proceedings by the Department of Labor (which enforces the FLSA), as well as potential investigations by state tax and workers’ compensation agencies. And as further discussed below, workers claiming to be misclassified may also pursue costly class action litigation, with the attendant risk of potentially very large liability verdicts. A misclassification finding therefore can place the very survival of a business at risk. This underscores the need for careful assessment before entering into any independent contractor arrangement.

c. Differences in Benefit Entitlement

Workers’ Compensation

Most state laws require U.S. employers to provide their employees with workers’ compensation insurance, which provides compensation for wage loss, medical treatment and death benefits in the event of a work-related injury or illness. No requirement exists to provide workers’ compensation coverage for independent contractors hired to perform services for the business. Since workers’ compensation coverage can be

costly, many businesses find it financially advantageous to hire independent contractors, where appropriate, in order to lower premiums.

Health Insurance

In 2010, the United States Congress passed the *Affordable Care Act* (“ACA”),¹⁹ colloquially known as “Obamacare,” which for the first time in the country’s history makes health insurance protection mandatory for most Americans. Beginning on January 1, 2015, employers with 50 or more full-time employees must offer health insurance coverage to their full-time employees.²⁰ Under the ACA, a “full-time” employee is one who works 30 hours or more per week or 130 hours or more per month. No mandate exists for businesses to provide similar coverage to part-time employees or independent contractors. Persons falling into these categories will instead be required to obtain individual coverage in the marketplace or incur a tax penalty.

Leave Benefits

The *federal Family and Medical Leave Act of 1993* (“FMLA”),²¹ which covers companies with at least 50 employees, allows eligible employees to take up to 12 weeks of unpaid leave in a 12-month period for certain family and medical reasons.²² These include the birth, adoption or placement for foster care of a child and incapacity due to an employee’s or family member’s serious health condition. In addition, employees may take leave for certain purposes in the event a family member is called to active duty or sustains injury or illness as a result of military service. The FMLA applies only to employees and affords no benefits to independent contractors.

Various states have statutes that provide leave benefits greater than, or in addition to, the FMLA. As with the FMLA, most of these state-level statutory benefits are restricted to individuals classified as employees.

Other Employee Benefits

Generally, U.S. employers are not legally mandated to provide other types of benefits to employees. Thus, except where state law provides otherwise, businesses need not offer vacation, sick leave, disability or retirement benefits to their employees, and when employers do provide such benefits, independent contractors are typically excluded. Some states offer state-funded benefits, such as disability payments, to employees. Independent contractors’ eligibility for such benefits would depend on the particular state law at issue.

The contractor/employee distinction is particularly important for employee benefit plans covered by ERISA, which can lose their tax-favored status if they cover independent contractors. Independent contractors generally are precluded from participating in a company’s tax-qualified retirement plans, because such plans can only cover employees. It would be permissible for an independent contractor to participate in a company’s health plans, assuming the insurance policy allows it, but if the company were to make premium payments on behalf of the independent contractor, the payments would be includable in the contractor’s gross income. Employees, by contrast, may exclude such payments from gross income.²³

Unemployment Compensation

Generally, a company is liable for making unemployment insurance withholdings from the compensation paid to employees (including temporary employees), but not from compensation paid to independent contractors. If a worker classified as an

independent contractor subsequently makes a claim for unemployment compensation benefits, the relevant state agency will likely re-examine this classification, and the employer may be held liable if the agency determines that the individual was misclassified and contributions should have been paid.

d. Differences in Protection from Termination

With the exception of the State of Montana, employment in the United States is deemed to be “at will” absent a written contract to the contrary. This means both employer and employee are free to terminate the employment relationship at any time, with or without notice, and for any or no reason. This basic common-law principle, however, is limited by an intricate framework of state and federal statutory and common-law rights providing employees – but not independent contractors – with protection against termination decisions that arise from an unlawful motive. Unlawful motives include discrimination based on an employee’s race, color, national origin, religion, age, gender, disability and other legally protected statuses, as well as retaliation against a worker for complaining of discrimination, for blowing the whistle on alleged illegal activity, for exercising legal rights to certain employee benefits, and for a myriad of other legally protected activities.

By contrast, the duration and termination of an independent contractor arrangement is generally regulated by contract. An independent contractor relationship is, by its very definition, one that is limited in duration and that ends upon completion of the project for which the contractor was hired. The parties may by agreement specify conditions on which the agreement may be terminated at an earlier time.

e. Local Limitations on Use of Independent Contractors

There are no laws that limit the use of independent contractors to specific purposes or circumstances. Rather, the primary limitation is the risk of misclassification. Increasingly, states are passing laws that create a presumption of employee status for individuals performing services in certain industries, such as construction, where misclassification has historically been the most prevalent. These statutes squarely place the burden on the employer to provide evidence that a worker is sufficiently independent to qualify as an independent contractor. The statutes generally impose civil and criminal penalties on employers who knowingly or willfully misclassify employees. Among the states that have passed such laws are Pennsylvania, Delaware, Colorado, Illinois, Minnesota, New York, and Maine. Other states are considering similar legislation.

In slight contrast to the state laws discussed above placing the burden on the employer to prove that a worker qualifies as an independent contractor, Arizona passed a law, Declaration of Independent Business Status (“DIBS”), effective August 6, 2016 allowing employers contracting with independent contractors to prove the existence of such a relationship through a signed declaration by the independent contractor. A declaration by the independent contractor is considered, under the law, a rebuttable presumption that an independent contractor relationship exists. Examples of declarations include the contractor’s acknowledgement that: he/she is paid per project and not hourly or through salary, not covered by employer health insurance or worker’s compensation, not restricted to perform services for other parties, and is not dictated by employer on how to perform services. The employer is not required to include such a declaration, and lack of such does not raise a presumption that an independent contractor relationship does not exist.²⁴ The Arizona statute stands in some tension with the 2015 DOL guidelines which advise that labels should not be a determinative factor in deciding whether an employee is a worker or independent contractor.

¹⁹ Patient Protection and Affordable Care Act of 2010, Public Law 111–148, 124 Stat. 119, codified as amended at scattered sections of the Internal Revenue Code and in title 42 of the United States Code.

²⁰ ACA § 6055, 6056. In July 2013, the deadline was extended by one year from January 2014 to January 2015.

²¹ 29 U.S.C. §§ 2601 *et seq.*

²² 29 U.S.C. §§ 2601 *et seq.*

²³ 26 U.S.C. § 106.

²⁴ Arizona’s new Declaration of Independent Business Status (DIBS) amends Title 23 of the Arizona Revised Statutes by adding two new statutes: A.R.S. § 23-10601 and A.R.S. § 23-1602.

In addition, the terms of collective bargaining agreements may impose limitations on the use of independent contractors with respect to the work performed by the bargaining unit. A company that hires independent contractors to do work covered by a union contract could be held liable for breach of the collective bargaining agreement and may risk the filing of an unfair labor practice charge with the National Labor Relations Board, which enforces labor law in the United States.

f. Other Ramifications of Classification

Wage-and-Hour Laws

The federal FLSA and similar state wage-and-hour laws afford many U.S. employees the right to be paid a minimum wage and overtime compensation for hours worked in excess of the statutory threshold.²⁵ Some states also have laws requiring employers to provide employees with paid rest periods and unpaid meal breaks. These statutory protections are available solely to employees. As a result, a company found to have misclassified workers as independent contractors may be liable for unpaid wages and, in particular, overtime compensation due to employees for hours worked in excess of the statutory threshold.

Labor Law

The federal NLRA protects employee rights to form unions and to engage in collective bargaining and other concerted activity, affords remedies to employees who have been harmed by any violation, and protects employees and union members against unfair bargaining practices.²⁶ By its express terms, the NLRA covers only employees and not independent contractors.²⁷ Independent contractors have no statutory collective bargaining rights.

Other Statutory Protections

Employees in the United States are entitled to a broad range of additional statutory protections under federal and state laws that prohibit workplace discrimination and harassment. Many statutes also provide relief from retaliation against employees who have exercised their statutory right to complain about or report unlawful activity or to obtain certain benefits of employment provided by law. At the federal level, these statutes include *Title VII of the Civil Rights Act of 1964*, which protects employees from discrimination on the basis of race, color, national origin, sex and religion;²⁸ the *Age Discrimination in Employment Act of 1967*, which protects employees against age discrimination;²⁹ and the *Americans with Disabilities Act of 1990*, which protects employees against discrimination based on disability.³⁰

In addition, the FMLA prohibits employers from interfering with employees' use of statutorily-guaranteed leave and from retaliating against employees who avail themselves of such leave.³¹ ERISA, in turn, makes it unlawful to discriminate against any employee for exercising any right under an employee benefit plan.³² These federal statutes are limited to employees and do not cover independent contractors.³³ Note, however, that in some states, state and local employment discrimination laws have been interpreted to cover certain independent contractors. Thus, it is critically important to be cognizant of the

²⁵ Employees classified as executive, professional and administrative employees, as well as certain other classes of employees, are generally exempt from these provisions.

²⁶ 29 U.S.C. §§ 151–169.

²⁷ 29 U.S.C. § 152(3); see also *Eastern, Inc. v. N.L.R.B.*, 60 F.3d 855, 857–858 (D.C. Cir. 1995) (holding that the jurisdiction of the NLRB extends only to the relationship between an employer and its “employees” and not to independent contractor arrangements).

²⁸ 42 U.S.C. §§ 2000 *et seq.*

²⁹ 29 U.S.C. §§ 621 *et seq.*

³⁰ 42 U.S.C. §§ 12101 *et seq.*

³¹ 29 U.S.C. § 2615.

³² 29 U.S.C. § 1140.

³³ See *Brown v. J. Kaz, Inc.*, 581 F.3d 175, 181 (3d Cir. 2009) (Title VII).

applicable jurisdiction.

Numerous statutes also afford various types of whistleblower protections – among them the Sarbanes-Oxley Act of 2002, which protects employees of publicly-traded corporations who report alleged shareholder fraud or violations of federal securities laws.³⁴ In most (but not all) cases, whistleblower protections may be unavailable to independent contractors. Federal and state occupational safety and health laws likewise in most cases apply only to employees.

Vicarious Liability

The United States recognizes the common-law doctrine of *respondeat superior*, under which an employer can be held liable for the negligent acts of its employees if the acts were committed in the scope of employment and in furtherance of the employer's business. By contrast, under the common law of most states, the hiring party has – with limited exceptions – no responsibility for the negligence of an independent contractor.³⁵ Liability can arise if a third party is physically harmed by an act or omission of the contractor pursuant to orders or directions negligently given by the hiring party, or because the hiring party failed to exercise reasonable care to retain a competent and careful contractor.³⁶ The risk of liability can be lowered significantly by hiring independent contractors, rather than employees, where permissible under applicable law.

g. Leased or Seconded Employees

One way to avoid the legal pitfalls of misclassification is to enter into an agreement with a third-party employee leasing or workplace management firm. Such an agreement typically provides that the staffing firm, not the business, is responsible for hiring, placing and terminating workers; ensuring appropriate tax payments are made and tax reporting is performed; providing workers' compensation insurance coverage; and offering employee benefits, if available, directly to employees. Where an outside vendor has been engaged, the company's responsibilities can be limited significantly, reducing the possibility that an employer-employee relationship will be found to exist.

There exists considerable variability in this area. Some staffing companies hire the workers as their own independent contractors and thus assume the risk of misclassification. Others perform the full panoply of functions traditionally associated with an employment relationship, such as withholding of income taxes, payment of Medicare and Social Security contributions, payment of workers' compensation and unemployment insurance premiums, provision of employee welfare and retirement savings benefits, performance management, and implementation of employee discipline, transfer and promotion decisions. Since companies must be well-informed about the ramifications of each arrangement, entering into an arrangement with a reputable and knowledgeable provider is of critical importance.

Using a staffing company is not a cure-all. Under various employment statutes, the client of a staffing agency is potentially considered a “joint employer” for purposes of liability, such as those prohibiting discrimination and harassment. In that case, an employee leasing arrangement will afford only limited liability protection. Additionally, some state laws regulating staff leasing companies may expressly require the staffing company and its client to agree that both will assume joint employer responsibility in specific aspects of the worker's employment.

For example, regulations implementing the FMLA provide that “[w]here two or more

³⁴ 18 U.S.C. § 1514A.

³⁵ See RESTATEMENT (SECOND) OF TORTS § 409.

³⁶ See RESTATEMENT (SECOND) OF TORTS §§ 410 *et seq.*

businesses exercise some control over the work or working conditions of the employee,” or where the work performed “simultaneously benefits two or more employers,” a joint employment relationship may exist.³⁷ A company will likely be considered a joint employer of employees supplied by a staffing agency and be subject to many of the requirements of the FMLA, if the company and the agency: (1) share control over the worker; (2) share the worker’s services; or (3) act in each other’s interest with regard to the worker. Indeed, some courts have found that a joint employment relationship exists for FMLA purposes anytime a staff leasing agency places employees with a client employer.³⁸

Where employee rights to welfare and retirement benefits governed by ERISA are concerned, the specific language of the benefit plan may control whether workers are entitled to participate in a client company’s plans. Several recent court decisions hold that when workers appear to be employees under the common-law test and the language of the plan does not expressly exclude individuals on the payroll of third-party contractors, the workers may be entitled to participate in the client company’s ERISA benefit plans.³⁹

h. Regulations of the Different Categories of Contracts

There is no regulatory scheme that governs employment contracts or independent contractor agreements. The parties are free to contract as they see fit, subject only to the provisions of the various employment laws discussed in the preceding sections. Many employees do not have written contracts, but are employed on an “at-will” basis. The details of an at-will employment relationship are often described in policies and procedures promulgated by the employer for all employees. Contractual disputes arising from independent contractor agreements are commonly resolved through litigation. Employment laws are enforced through agency actions such as audits, investigations and legal proceedings, as well as through private litigation initiated by employees claiming to be aggrieved.

III. RE-CHARACTERISATION OF INDEPENDENT CONTRACTORS AS EMPLOYEES

a. Laws and Guiding Principles

As discussed in Section I of this chapter, classification of independent contractors and employees is subject to an intricate framework of statutory and common-law approaches. A fundamental principle, however, is that courts must undertake a comprehensive examination of all relevant facts. No single factor is dispositive. Instead, careful balancing of all relevant factors is required to reach a determination based on the specific situation at hand.

That said, there are common themes that run through each of the various tests. Although an independent contractor agreement should be detailed and carefully documented, the written agreement between the parties never controls the outcome. Certainly, the parties’ intent matters. However, it is the actual implementation and the realities of the parties’ performance that determines how courts will characterize the relationship. For purposes of the common-law and Right to Control tests, the focal point of the analysis will be the company’s ability to control and direct the manner and sequence of the worker’s

³⁷ 29 C.F.R. § 825.106(a).

³⁸ See *Grace v. USCAR*, 521 F.3d 655 (6th Cir. 2008); 29 C.F.R. § 825.106(b)(1).

³⁹ See, e.g., *Curry v. CTB McGraw Hill, LLC*, No. 06-CV-15397, 296 Fed. App’x 563 (9th Cir. Oct. 9, 2008) (“we have not held that all common law employees are entitled to benefits under ERISA . . . , [i]nstead we look to the terms of the plans at issue to determine who is entitled to coverage”) *Schultz v. Stoner*, No. 00-CV-439, 2009 BL 36510 (S.D.N.Y. Feb. 24, 2009); *Bendsen v. George Weston Bakeries Distribution, Inc.*, 2008 BL 216258, No. 09-CV-50 (E.D. Mo. Sept. 26, 2008).

performance. Under the Economic Realities test, the analysis turns on the degree of the worker’s dependence on the company. At bottom, the fundamental question under any test is whether the facts demonstrate that the worker is truly in business for him- or herself. If so, an independent contractor relationship exists.

b. The Legal Consequences of a Re-Characterisation

When independent contractors are reclassified as employees, employers may be subject to payment of back income tax withholdings and Social Security and Medicare tax contributions, as well as for penalties for misclassification. Employers also risk potential claims by employees for unpaid hourly and overtime compensation, and past workers’ compensation and employee benefits liabilities. In addition, government agencies may conduct audits and investigations and impose additional obligations, combined with penalties and interest for noncompliance. Moreover, only employees, and not independent contractors, have the right to form unions. Reclassification thus entails the risk of greater unionizing activities and potential collective bargaining obligations if such activities are successful.

In some situations, reclassification of independent contractors as employees may increase the number of employees and render an employer subject to other laws that were previously inapplicable, because the employer did not meet the threshold. For example, the FMLA covers only employers with at least 50 employees, while most federal employment discrimination laws cover only those employers who have at least 15 or 20 employees, depending on the statute. Employers with 100 or more employees must additionally file annual EEO-1 reports with the United States Equal Employment Opportunity Commission. Other reporting requirements similarly come into play once a particular employee size threshold is crossed. Employers thus must take careful account of the implications once coverage under a particular statute is triggered.

c. Judicial Remedies Available to Persons Seeking ‘Employee’ Status

If a worker believes he or she has been incorrectly classified as an independent contractor, the worker can request a determination of worker status for purposes of federal employment taxes and income tax withholdings from the IRS. In the event of a determination that the worker was misclassified, the business is sent a letter notifying it of its obligation to pay employment tax and to adjust any previously filed employment tax returns accordingly. Workers may also file complaints for unpaid wages with the U.S. Department of Labor, which enforces the FLSA. An individual complaint will result in an administrative investigation, but may also trigger a broader audit of independent contractor classification practices for similarly-situated workers. When the agency finds that misclassification has occurred, enforcement actions may result seeking relief not only on behalf of the complaining individual, but also for other misclassified workers throughout the organization.

Apart from seeking relief through administrative agency determinations and enforcement actions, workers seeking employee status may also file civil lawsuits. At the state level, an increasing number of state legislatures are enacting misclassification statutes, many of which grant workers the right to file a private suit for misclassification, with varying remedies. Some laws are limited to particular industries, such as constructions. Others have broad applicability. For example, Massachusetts’ misclassification statute applies broadly to a wide range of industries and places the burden on the employer to prove each element of a more stringent version of the ABC Test discussed in prior sections.⁴⁰ In addition to the penalties imposed by other laws, the Massachusetts statute authorizes the Attorney General to impose substantial civil and criminal penalties, and in certain circumstances, to debar violators from public works contracts.

⁴⁰ See Mass. Gen. Law ch. 149, § 148B.

Regardless of whether a state law affords the right to file an action for misclassification, workers may also bring lawsuits under many employment laws, claiming they were improperly classified and treated as independent contractors. For example, the FLSA permits individuals to file “collective actions” – actions filed by a plaintiff as the representative of a class of others similarly situated who elect to participate – in order to seek unpaid wages and overtime compensation based on their alleged independent-contractor misclassification. Under ERISA, persons may file both individual and class-action lawsuits to contest eligibility determinations denying them benefits as a result of having been designated as independent contractors. Civil lawsuits for discrimination, retaliation or interference with benefits can also be filed under various non-discrimination statutes such as Title VII, ADEA and ADA, under the FMLA and other various state and federal whistleblower statutes, as well as under various common-law theories protecting employees, based on the assertion that the contractor should have been classified as an employee protected by the statute.

Class and collective actions asserting misclassification under the FLSA, ERISA, and related laws represent a significant source of potential liability for employers. In some cases, especially where the alleged misclassification has affected broad job categories with numerous incumbents, the potential class size, and with it the potential liability exposure – not to mention the costs of defense – can be truly enormous. One recent case, for example, combined over 42 class action lawsuits filed in 28 states on behalf of thousands of delivery drivers for FedEx Ground, who alleged they had been misclassified as independent contractors and sought reimbursement of business expenses as well as payment of back wages and overtime.⁴¹ At the end of 2010, a federal district judge ruled in favor of FedEx Ground under the laws of 20 of the 28 states. That ruling remains on appeal. In the meantime, individual state class actions against FedEx Ground continue to progress, often with divergent and inconsistent results, depending on the applicable state law.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

The remedies and penalties flowing from independent contractor misclassification in the United States vary depending on the particular statute implicated in a given legal proceeding. A synopsis of penalties and damages based on federal law appears below. It is important to recognize, however, that the availability of collective and class action mechanisms under many statutes can expose employers to liability verdicts of potentially massive proportions.

Tax Considerations

The federal Internal Revenue Code (“IRS Code”) imposes significant potential liability on businesses that fail to withhold and pay employment taxes as a result of employee misclassification. In addition to payment of back taxes and accrued interest,⁴² if an employee is found to have been misclassified in an IRS audit, a company found to be in violation of federal tax law could be held liable for substantial penalties based on the company’s failure to withhold and collect federal income tax, FICA, and FUTA taxes (accruing monthly up to 25% of the net amount due); for failure to file timely and accurate tax reports (also accruing monthly up to 25%); as well potentially for civil fraud.⁴³ A knowing violation of the statute might also result in criminal prosecution.⁴⁴

The good news for employers is that in some cases, assuming the misclassification was not willful, liability can be avoided under the safe harbor provision established by section

41 *In re FedEx Ground Package System, Inc. Employment Practices Litigation*, Civil Action No. 3:05-MD-527 (RM) (MDL-1700), in the United States District Court for the Northern District of Indiana, Fort Bend Division.

42 26 U.S.C. § 3509(a).

43 See 26 U.S.C. chapter 68.

44 26 U.S.C. §§ 7202, 7204.

530 of the Revenue Act of 1978.⁴⁵ This provision allows an employer to continue to treat a worker as an independent contractor even if the worker would have been treated as an employee under the Right to Control test, if three conditions are met: (i) the employer has filed all required returns reporting payments to the worker as an independent contractor; (ii) the employer has not treated the worker or any similarly situated worker as an employee; and (iii) the employer had a “reasonable basis” to have treated the worker as an independent contractor. A “reasonable basis” can include reliance on prior case law, a past IRS audit, industry practice, as well as other reasonable considerations. If all of these requirements are satisfied, the employer’s liability for payment of employment taxes, interest and penalties may be terminated even though the worker is properly classified as an employee.

Wage-and-hour Considerations

Under the FLSA, employees (other than those exempt from the relevant provisions of the FLSA) must be paid no less than a specified minimum wage for each hour worked, as well as an additional premium of one-half the employee’s regular rate for each hour of overtime work. Independent contractor misclassifications can result in liability for unpaid wages and overtime wages, an equal amount as liquidated damages, attorneys’ fees and costs. Also, because the statute permits lawsuits to be brought as collective actions on behalf of similarly-situated others, an employer’s liability exposure can be quite significant if a large group of workers is found to have been improperly classified as independent contractors.

Employee Welfare and Retirement Benefits

Employers who misclassify employees as independent contractors and deem them ineligible for participation in the company’s employee benefit plans can incur significant tax penalties for failing to offer or provide sufficient coverage or make necessary premium payments. In addition, such employers run the risk of individual and class action lawsuits on behalf of all misclassified employees seeking rights to benefits.⁴⁶ Class action lawsuits may also be filed under the federal Family and Medical Leave Act, which provides employees, but not independent contractors, a right to unpaid leave for certain family and health reasons and protects against termination for having taken such leave.

Workers’ Compensation Insurance

Misclassification of employees as independent contractors for workers’ compensation purposes can result in an award of benefits, as well as assessments of civil penalties and potential criminal liability, depending on the particular state’s workers’ compensation statute.

State Misclassification Statutes

Many state misclassification laws impose civil penalties and restitution requirements, particularly if the employer is found to have knowingly misclassified workers. Such statutes may also grant workers a private right of action.⁴⁷

IV. HOW TO STRUCTURE AN INDEPENDENT CONTRACTORS RELATIONSHIP

a. How to Properly Document the Relationship

Given the potentially devastating consequences of misclassification, every independent contractor relationship should be carefully and fully documented. Before entering into

45 Pub. L. No. 95-600, § 530, 92 Stat. 2763, 2885–86, as amended. Although not directly a part of the Internal Revenue Code, the text of section 530 is included in the notes accompanying 26 U.S.C. § 3401(a).

46 See 29 U.S.C. § 1132(a)(1).

47 See, e.g., the Massachusetts Misclassification Act, Mass. Gen. Law ch. 149, § 148B; the Maryland Workplace Fraud Act, Md. Code Ann., Lab. & Empl. §§ 3-901 to -920; the Kansas misclassification statute, Kan. Stat. Ann. § 44-766(a); and the New Mexico misclassification law, N.M. Stat. Ann. § 60-13-3.1(C).

the relationship, the hiring company should obtain basic information and supporting documentation from the prospective contractor, including:

- the structure of the independent contractor's business (e.g., sole proprietorship, limited liability company, corporation, partnership, etc.);
- whether the independent contractor has any employees or work under subcontracts;
- whether the independent contractor has performed similar services for other companies;
- whether and where the independent contractor maintains an office (other than the contractor's home);
- how and where the contractor markets and advertises services;
- the types of insurance coverage maintained by the independent contractor; and
- the contractor's tax identification number.

If the information obtained demonstrates to the hiring party's satisfaction that the prospective worker meets basic prerequisites to qualify as an independent contractor and that the work to be performed suits the criteria for an independent contractor arrangement, the next step normally is to document the relationship in an independent contractor agreement. That agreement should, at a minimum, specify the following:

- the duration of the relationship (which should be tied to the duration of the project for which the worker is retained);
- the nature and scope of services to be provided (which should be different from those performed by rank-and-file employees);
- the manner and conditions for payment of compensation (e.g., a fixed sum upon completion of the project or identified milestones);
- that the service provider is an independent contractor and not an employee;
- that the independent contractor will not be eligible to participate in any employee benefits;
- that the independent contractor, and not the company, will be responsible for payment of all applicable taxes and legally required contributions;
- that the independent contractor will provide his or her own workers' compensation coverage;
- what other insurance coverage the independent contractor is required to carry for the duration of the relationship;
- that the contractor is free to set his or her own hours of work and to determine in what manner and sequence the work should be completed;
- that the independent contractor will supply and use his or her own equipment;
- that the contractor will be required to pay his or her own business expenses;
- that the independent contractor is free to hire his or her own employees;
- the conditions on which the relationship may be terminated and the consequences of early termination, including any notice requirements and potential penalties; and
- any desired indemnification (e.g., independent contractor's agreement to indemnify and defend the company in the event of loss, damage or liability caused by the contractor's own negligence).

Given the great variability in relevant classification testing, particularly in light of the many different approaches under state law, it is strongly recommended that the agreement be reviewed by counsel, in light of applicable standards and actual practice. Careful structuring of the independent contractor agreement is imperative to ensure that the agreement itself does not contain terms suggesting that the business has a right to control the manner and means by which the worker performs the tasks set forth in the contract.

b. Day-to-Day Management of the Relationship

Even the most well-drafted independent contractor agreement is of little value if it does not accurately reflect reality. Companies should make every effort to grant independent contractors the level of independence required to preserve the integrity of an independent contractor classification. Whenever possible, the independent contractor should be a separately incorporated business. Ideally, contractors should be able to set their own hours, have freedom in selecting the site at which work is performed and be free to offer their services to other potential clients. Day-to-day supervision and direction of the contractor's work in particular should be avoided.

Contractor work assignments should not mirror those given to employees. Rather, employers should carefully and clearly define projects designated for independent contractors, and set specific start and end dates. Any internal evaluation of the performance of independent contractors should focus on the quality and acceptability of the final work product rather than the manner in which it was produced. Under no circumstances should an employer use its employee performance review process to evaluate the work done by an independent contractor. It is also advisable to require independent contractors to provide periodic progress reports and to submit regular invoices as defined targets are met. Moreover, independent contractors should never be paid as part of the company's regular employee payroll.

Where it is not possible in practice to conform the relationship to the legal requirements, employers may wish to consider alternatives such as re-documenting the relationship to align it with the applicable standards, or retaining a third-party staffing or workforce management company. Although not a panacea, the use of third-party staffing organizations can provide a meaningful buffer to liability under many circumstances and could greatly simplify day-to-day management of the relationship.

V. TRENDS AND SPECIFIC CASES

a. New or Expected Developments

Recent years have seen vastly stepped-up enforcement efforts on the part of federal and state government agencies seeking to remedy revenue shortfalls in the wake of the economic downturn that began in 2008. All the while, the plaintiff's bar has increasingly targeted employer use of independent contractors, and the number of class action lawsuits alleging misclassification under federal and state laws has risen steeply. All these developments have placed companies who enter into independent contractor relationships at substantial risk of adverse findings and judgments.

Increased Internal Revenue Service Enforcement and Voluntary Settlement Programs

In 2010, the IRS launched an intensified enforcement program involving widespread audits of businesses to uncover misclassification issues. A year later, the agency announced a new Voluntary Classification Settlement Program ("VCSP"), allowing employers to voluntarily reclassify workers previously treated as independent contractors without incurring tax obligations or penalties for past misclassifications. Under the VCSP, employers receive immunity from IRS misclassification audits in exchange for payment of 10% of the employment tax liability for misclassified workers for one year. Interest and penalties are waived. To be eligible to participate in the VCSP, an employer must, among other matters, have consistently treated the affected workers as nonemployees in the past and have filed the required Forms 1099 for these workers for at least the previous three years.

Participation in the VCSP has been relatively sparse, most likely because the VCSP resolves only an employer's potential federal tax liability, but not any potential liability arising from misclassification under state tax, employee benefits, wage-and-hour, workers' compensation and other employment-related laws. Concerned that participation in the program may highlight the existence of potential misclassification issues and invite further audits and lawsuits, many companies have remained wary.

Stepped-up Interagency Cooperation

In September 2011, the United States Department of Labor announced that it had entered into an unprecedented Memorandum of Understanding ("MOU") with the IRS. The MOU provides the foundation for future cooperation and information sharing among the two agencies to facilitate enhanced enforcement of federal tax, wage-and-hour, workplace safety and benefits laws in response to alleged misclassification of employees.

Several states have likewise formed interagency and joint task forces to combat the perceived misclassification problem. The task forces are generally responsible for facilitating the sharing of information and resources among the relevant administrative agencies, developing joint investigative and enforcement strategies, and encouraging the reporting of alleged violations. Agencies in at least 14 states have additionally signed MOUs with the federal Labor Department's Wage-and-hour Division. At the same time, 34 state agencies now share information concerning misclassification issues with the IRS as part of the IRS Questionable Employment Tax Practices initiative, which aims to identify unlawful employment tax practices.

As a result of this vastly improved communication and collaboration among different federal and state agencies, a single audit by one agency may now result in investigations and enforcement actions at multiple levels under multiple different laws, each with its own potential penalties and other consequences. This means that misclassification of even a single position carries the risk of expansive agency enforcement. As agencies have intensified the publicity of enforcement proceedings, such actions now more easily attract the attention of the plaintiff's bar, resulting in a greater risk of private lawsuits.

Department of Labor (DOL) Updates and Guidelines

On December 19th, 2016 the Department of Labor ("DOL") updated its Independent Contractor misalignment webpage, reissuing its resources on independent contractor misclassification and grouping these resources together with resources from other federal and state agencies on the issue. Although no information provided is new, it signifies the DOL's continued focus on the issue of independent contractor misclassification, bringing awareness to both workers and employers of this issue.

• DOL Guidance On Application of the Economic Realities Test and the FLSA⁴⁸

On July 15, 2015, in light of a perceived increase in misclassification of employees as independent contractors⁴⁹ largely due to how businesses are being restructured of late, the Department of Labor (the government agency which enforces the FLSA) issued guidelines regarding the application of the FLSA's definition of employee as "to suffer or permit to work" standard to the identification of workers misclassified as independent contractors. The DOL clarified that the factors found in the Economic Realities Test should be applied in consideration of the broad scope of the FLSA's "suffer or permit" standard, which was "specifically designed to ensure as broad a scope as coverage as possible". The FLSA's statutory definitions rejected the more narrow common law control test, in deference

⁴⁸ Administrator's Interpretation No. 2015 Issued by Administrator David Weil, The Application of the FLSA's "Suffer or Permit" Standard in the Identification of Employees Who are Misclassified as Independent Contractors, available at https://www.dol.gov/whd/workers/Misclassification/AI-2015_1.pdf.

⁴⁹ According to the Bureau of Labor Statistics, approximately 3.4 million workers are classified as independent contractors when they should be classified as employees. 10 – 20% of employers misclassify at least one worker.

to the economic realities test which should read in line with the FLSA's "suffer or permit" standard which "stretched the meaning of 'employee' to cover some parties who might not qualify as such under a strict application of traditional agency law principles"⁵⁰. Thus the Economic Realities Test should be construed with awareness to the FLSA's "overarching principle" of broad coverage for workers. The main analysis rests on whether the worker is economically dependent on the employer as opposed to in business for him/her self. If the worker is economically dependent on the employer, then the worker is an employee.

Guiding the determination of whether a worker is economically dependent on the employers are the factors from the Economic Realities Test. The DOL provides interpretation of the six factors of the Economic Realities Test, factor-by-factor, citing case law mentioned throughout this article. "All of the factors must be considered in each case, and no one factor (particularly the control factor) is determinative of whether a worker is an employee," David Weil, DOL Administrator said. He emphasized that the factors "should not be applied in a mechanical fashion, but with an understanding that the factors are indicators of the broader concept of economic dependence." Moreover the label given to a worker by his employer, or even agreed upon by both the worker and employer, is not determinative. The DOL advised that this same analysis should be applied when considered the status of a worker under the Family and Medical Leave Act, and the Migrant and Seasonal Agricultural Worker Protection Act, both of which use the FLSA's definition of "employ". In addition to the factors of the Economic Realities Test, the DOL also provides the following factors for consideration of whether a worker is an employee or independent contractor.⁵¹

- the method of payment
- how free the employer is to replace one employee with another
- whether the alleged independent contractor is listed on the payroll with appropriate tax deductions
- whether the possible employer must approve the employees of the alleged independent contractor
- whether the possible employer keeps the books and prepares the payroll for the possible employee
- whether the alleged independent contractor is assigned to a particular territory without freedom of movement
- whether the independent contractor has an independent economic interest in his or her work
- how the respective tax returns of the parties list the compensation paid

In addition, the DOL provides a list of factors, which it finds "irrelevant" to the determination of a worker as an employee or independent contractor⁵²:

- whether the worker has a license from a state or local government
- the measurement, method, or designation of compensation
- the fact that no compensation is paid and the worker must rely entirely on tips
- the place where the work is performed
- the absence of a formal employment agreement

Although the DOL guidelines, legally, contain nothing new, they signify a heightened focus on the concept of "economic dependence" in the employee v. independent contractor analysis, as well as confirmation that the issue of independent contractor misclassification is a key issue for the DOL, and one which employers should analyze with caution.

⁵⁰ *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 326 (1992).

⁵¹ See U.S. Dep't of Labor, Field Operations Handbook ch. 10, §§ 10b05(a), 10b07(a) (1993) (FOH 2.10b).

⁵² See U.S. Dep't of Labor, Field Operations Handbook ch. 10, § 10b07(c)(1993) (FOH 2.10b).

Proposed Federal Legislation

• Independent Contractor Tax Fairness and Simplification Act of 2015⁵³

In May 2015, Representative Erik Paulsen of Minnesota introduced the Independent Contractor Tax Fairness and Simplification Act which expressly states that the term “employment status” shall mean the classification of an individual as an employee or IC under the common law rules, and would codify a new form of “safe harbor” if worker met all four of the following factors:

- incurs significant financial responsibility for providing and maintaining equipment and facilities;
- incurs unreimbursed expenses or risks income fluctuations because remuneration is “directly related to sales or other output rather than solely to the number of hours actually worked or expenses incurred”;
- is compensated on such factors as percentage of revenue or scheduled rates and not solely on the basis of hours or time expended; and
- “substantially controls the means and manner of performing the services” in conformity with regulatory requirements, or “the specifications of the service recipient or payor and any additional requirements” in the parties’ written IC agreement.

This bill has a narrow scope, limited to independent contractors who bill for services such as drivers and message couriers. The bill would have no impact on whether a worker was deemed employee or independent contractor under the FLSA. Similar bills have been proposed in the past, and no congressional action was taken⁵⁴.

Other proposed bills relating to independent contractor misclassification include – the Fair Playing Field Act (introduced in 2010, and again in 2012, and 2013)⁵⁵, the Payroll Fraud Prevention Act (introduced in 2011, and again in 2013, and 2014)⁵⁶, and the Employment Misclassification Act (introduced in 2008, and again in 2010 and 2011)⁵⁷. None of these bills have resulted in enactment.

b. Recent Amendments to the Law

Emergent State Misclassification Legislation

As state agencies are collaborating with the federal government at increasing rates to curb misclassification, a significant number of state legislatures have also entered the fray by passing legislation. Some of the new laws are specific to certain industries where worker misclassification is perceived to have been particularly rampant. For example, in 2007, New Jersey passed the Construction Industry Independent Contractor Act.⁵⁸ The statute creates a rebuttable presumption that full-time construction workers are employees and not independent contractors, for purposes of many New Jersey labor and employment statutes. Penalties for violations include suspension of the contractor’s registration, “stop-work” orders, and civil fines. Similar statutes have been enacted in

Delaware,⁵⁹ Maine,⁶⁰ New York,⁶¹ Pennsylvania,⁶² as well as several additional states.

Other states have laws that apply more generally to all industries. California’s Independent Contractor Law, for example, which took effect in 2012, prohibits any form of “willful misclassification,” and makes it unlawful for employers to charge misclassified employees for business expenses and to make improper deductions from their pay. The statute not only imposes harsh penalties on violators, but also holds outside non-legal consultants jointly liable for “knowingly advis[ing] an employer to treat an individual as an independent contractor to avoid employee status” if it turns out the individual was not in fact an independent contractor.⁶³ Other states that have enacted misclassification laws within the past decade include Colorado,⁶⁴ Connecticut,⁶⁵ Illinois,⁶⁶ Louisiana,⁶⁷ Maryland,⁶⁸ Massachusetts,⁶⁹ New Hampshire,⁷⁰ and New Mexico.⁷¹ In September 2014 California also passed Assembly Bill No. 1897, adding a section to the Labor Code regarding labor contracting and client liability⁷². This increases liability risk for companies that use workers supplied by “labor contractors” that fail to pay all wages due to the workers. The law requires client employers to “share with a labor contractor all civil legal responsibility and civil liability for all workers supplied by that labor contractor for . . . the payment of wages and failure to secure workers’ compensation coverage.” Three key exclusions in the law include: 1) those exempt from overtime payment (executive, administrative, or professional employees), 2) business with workforces of less than 25 individuals or a workforce with less than 5 independent contractors, and 3) bona fide independent contractors supplied by a labor contractor.

As discussed earlier Arizona passed a law, Declaration of Independent Business Status (“DIBS”), effective August 6, 2016 allowing employers contracting with independent contractors to prove the existence of such a relationship through a signed declaration by the independent contractor. A declaration by the independent contractor is considered, under the law, a rebuttable presumption that an independent contractor relationship exists. The employer is not required to include such a declaration, and lack of such does not raise a presumption that an independent contractor relationship does not exist.⁷²

Recent Cases

Companies with a business structure, which either uses independent contractors to supplement its workforce or maintains a primarily independent contractor workforce, are increasingly targeted by plaintiffs’ class action lawyers. Both large and small business organizations have become targets. Although no industry is free from this type of lawsuits some industries are more vulnerable than others. Industries that are particularly vulnerable include on-demand businesses, and Silicon Valley startups.

In March 2015 federal court judges in California issued two separate decisions in independent contractor misclassification class action lawsuits⁷³. Both *O’Connor v. Uber Technologies, Inc.* and *Cotter v. Lyft* are class actions brought by drivers of the respective companies who allege that Uber and Lyft misclassified them as independent contractors instead of employees, depriving them of employee rights and benefits. In both cases the

⁵³ 113th Congress, 2d Session, H.R. 4611. Amendment to the FLSA, available at <https://www.gpo.gov/fdsys/pkg/BILLS-113hr4611ih/pdf/BILLS-113hr4611ih.pdf>.

⁵⁴ See Independent Contractor Tax Fairness and Simplification Act of 2012, H.R. 4611, available at <https://www.gpo.gov/fdsys/pkg/BILLS-112hr6653ih/pdf/BILLS-112hr6653ih.pdf>.

⁵⁵ Fair Playing Field Act of 2013, S.1706, available at <https://www.gpo.gov/fdsys/pkg/BILLS-113s1706is/pdf/BILLS-113s1706is.pdf>.

⁵⁶ See Payroll Fraud Prevention of 2013, S.1687 available at <https://www.gpo.gov/fdsys/pkg/BILLS-113s1687is/pdf/BILLS-113s1687is.pdf>.

⁵⁷ Employment Misclassification Prevention Act of 2008, H.R. 6111, available at <https://independentcontractor-compliance.com/legal-resources/state-ic-laws-and-selected-bills/>.

⁵⁸ N.J.S. 34:20-1 to 34:20-11.

⁵⁹ Del. Code Ann. tit. 19, § 3501.

⁶⁰ Me. Rev. Stat. Ann. § 105-A.

⁶¹ N.Y. Lab. Law art. 25-B.

⁶² 43 P.S. §§ 933.1 -- 933.17.

⁶³ Cal. Lab. Code Ann. §§ 226.8, 2753.

⁶⁴ Colo. Rev. Stat. § 8-70-115(b).

⁶⁵ Conn. Gen. Stat. § 31-222(a)(1)(B)(ii).

⁶⁶ 820 ILCS 185/1-999.

⁶⁷ La. R.S. 23:1021.

⁶⁸ Maryland Gen. Stat. 9-402.1.

⁶⁹ Mass. Gen. Laws ch. 149, § 148B

⁷⁰ RSA 281-A:2.

⁷¹ N.M. Gen. Stat. § 51-1-42.

⁷² Assembly Bill No. 1897, Chap. 728, Sec. 2810.3.

court denied motions and ruled that a jury would decide whether the workers are considered independent contractors or employees. Moreover both courts concluded that some of the factors signaled an employee designation, while other factors signaled an independent contractor designation. Both companies allow the workers to determine when and how much they want to work, and whether to accept or reject rides. On the other hand, both companies expressly reserve the right to terminate the relationship if the driver's user rating is deemed low or for any reason at all (a key employee status factor). As a result of these decisions, Uber, Lyft, and any "on demand" business (an increasingly popular business model) are at risk if they do not structure their employee – independent contractor relationship in a manner which remains in line with federal and state requirements. This however does not mean that companies cannot prevail on IC misclassification claims, as the *Uber* court noted that recent California cases found in favor of the employer, where "all the factors weighed and considered as a whole establish that an [individual] was an independent contractor and not an employee".

In August 2014, the ninth circuit issued two decisions regarding Fedex Ground drivers class actions in Oregon⁷³ and California⁷⁴. The drivers sought unpaid wages, reimbursement of unpaid driving expenses and similar types of state law damages. The Ninth Circuit looking at the two class actions together analyzed the Fedex Ground contract (Operating Agreement) that each driver entered into, in addition to standard Fedex policies and procedures. The Court concluded that the Fedex Ground drivers were employees and not independent contractors on grounds that: Fedex has the right to and ultimately controls driver appearance, can and does control driver vehicles, can and does control the time drivers work, can and does control when and how drivers deliver packages, and requires drivers to "conduct all business activities... with proper decorum at all times". The significance of these decisions is that despite reliance on an explicit Independent Contractor Agreement, upon close scrutiny the Court found several key factors out of line with the legal standard for an independent contractor classification.

In June 2015 Fedex announced that its Ground Division "has reached an agreement in principle with [drivers] in the independent contractor litigation that is pending in California [federal court] to settle for \$228 million dollars". To prevent a similar outcome companies should: 1) restructure the independent contractor relationship in a manner which still serves business objectives, 2) redraft independent contractor contracts in close consideration of federal and state laws regarding independent contractor misclassification, and 3) reimplement the employer – independent contractor relationship in a manner consistent with the restructure and redraft.

Many tax- and employment-related statutes implicated by misclassification distinguish between businesses that believe in good faith that they have correctly interpreted applicable classification standards and those that have willfully violated the law. However, this is not always the case. In *Somers v. Converged Access, Inc.*,⁷⁵ the Massachusetts Supreme Court held that the state's independent contractor law is a strict liability statute, which means it is irrelevant whether an employer who misclassified an employee acted in good faith. The plaintiff, a temporary worker, filed a private lawsuit alleging violation of the

Massachusetts statute after the company failed to hire him for a permanent position.

The company argued that the plaintiff had sustained no damages, because he actually realized greater earnings than he would have had as an employee. The Supreme Court disagreed, observing that the plaintiff had not received the vacation, holiday, or overtime

⁷³ Arizona's new Declaration of Independent Business Status (DIBS) amends Title 23 of the Arizona Revised Statutes by adding two new statutes: A.R.S. § 23-10601 and A.R.S. § 23-1602.

⁷⁴ *O'Connor v. Uber Technologies, Inc.*, No. 3:13-cv-03826-EMC (N.D. Cal. Mar. 11, 2015); *Cotter v. Lyft, Inc.*, No. 3:13-cv-04065-VC (N.D. Cal. Mar. 11, 2015).

⁷⁵ *Slayman v. FedEx Ground Package System, Inc.*, No. 12-35525 and 12-35559.

pay paid to employees. If the plaintiff could demonstrate that he was a misclassified employee, the Massachusetts statute would thus entitle him to recover treble damages for any lost wages and other benefits.

The seminal misclassification case under federal tax and benefits laws is *Vizcaino v. Microsoft Corporation*.⁷⁶ The case involved a group of workers Microsoft had classified as independent contractors and referred to as "freelancers." The freelancers were compensated at an hourly rate that was higher than the wage paid to employees performing similar work, were paid through Microsoft's accounts payable department rather than its payroll department, wore different badges and were not included in company functions. Despite these efforts to distinguish "freelancers" from regular employees, however, the IRS determined, following a classification audit, that the freelancers had been misclassified and were actually employees.

This conclusion prompted an ERISA class-action lawsuit by the freelancers, who demanded that Microsoft allow them to participate in a variety of employee benefits, including two of the company's employer-sponsored ERISA retirement plans. On appeal, the federal Ninth Circuit Court of Appeals noted that the freelancers could not be materially distinguished from Microsoft's remaining workforce: they often worked on teams with regular employees, they performed the same functions, they shared the same supervisors, and they worked the same hours. Microsoft then conceded that the workers were employees under the common-law test. The company argued, however, that the plan administrator had correctly refused to award benefits under the retirement plans, because the workers had agreed in their independent contractor agreements that they were not entitled to participate.

The court disagreed. The mere fact that the agreements labeled the workers as "independent contractors" was not dispositive, the court held, and the agreements were ultimately based on a mutual mistake and unenforceable. Accordingly, Microsoft was directed to fund the workers' retirement benefits retroactively. The case continued through several appeals, but was ultimately settled for close to U.S. \$97 million.

The Microsoft decision stands in sharp contrast to the decision by the federal Tenth Circuit Court of Appeals in *Capital Cities/ABC, Inc. v. Ratcliff*.⁷⁷ Like the workers in Microsoft, the plaintiffs in Ratcliff had signed independent contractor agreements affirming that they were not entitled to participate in the company's ERISA benefits plans. The court of appeals found that the agreements had been voluntarily executed and that it was therefore immaterial whether the workers could be deemed employees under common law. Since the workers had voluntarily relinquished their right to receive any benefits under the company's employee benefit plans, the court held that the terms of the agreement controlled and should be given effect.

The inconsistent holdings in Microsoft and Ratcliff highlight the importance of context and jurisdiction when evaluating any independent contractor relationship in the United States.

VI. BUSINESS PRESENCE ISSUES

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

A foreign entity with a permanent establishment in the United States may be subject to U.S. federal taxation. As a general rule, foreign corporations are subject to federal income

⁷⁶ *Alexander v. FedEx Ground Package System, Inc.*, No. 12-17458 and 12-17509.

⁷⁷ 454 Mass. 582, 590-591 (Mass. 2009).

tax on income that is effectively connected with a U.S. trade or business.⁷⁸ Such income may, however, be subject to exemption if a tax treaty so provides.⁷⁹ A common tax treaty exemption limits federal income taxation to amounts attributable to a permanent establishment maintained by the foreign entity in the United States. Such an exemption exists, for example, under the tax treaty between the United States and Canada.⁸⁰

Under the terms of this and other treaties containing such an exemption, a permanent establishment exists if the foreign company maintains in the United States either (1) a “fixed place of business” or (2) employees or “dependent agents” who have, and habitually exercise, authority to conclude contracts on behalf of the foreign company. By contrast, no permanent establishment is created if business is carried out through a broker, general commission agent, or other independent agent acting in the ordinary course of their business.

Court decisions interpreting these provisions are sparse. However, consistent with the language of the applicable treaty, courts customarily distinguish between an independent agent or contractor, retained to perform a specific project without authority to contract on behalf of the foreign principal, and a dependent agent who has such authority.⁸¹ In other words, independent agents or contractors who operate in the normal course of their own business and merely represent the products or services of the foreign resident generally do not create a permanent establishment of the foreign resident. On the other hand, when an agent is both legally and economically dependent on the foreign company, the presence of the agent is likely to give rise to a permanent establishment.⁸²

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

As discussed in the preceding section, tax treaties between the United States and many other countries provide an exemption from U.S. federal taxation for income derived by a foreign corporation from a U.S. trade or business if the foreign corporation lacks a permanent establishment in the United States. Treaties differ in their definition of “permanent establishment,” and the factors indicating the existence of a permanent establishment vary. Very commonly, however, the presence in the United States of a fixed place of business of the foreign entity or of employees of the foreign entity who habitually exercise the authority to bind the foreign company contractually will reflect the existence of a permanent establishment.

It is important to recognize that the federal government has no authority to enter into tax treaties with other countries that affect individual states. Each state has its own laws and criteria that determine when and under what circumstances a foreign company is considered to be transacting business in the state and thereby potentially subject to state taxation and regulation. It is commonly agreed that when a company exploits the state’s marketplace – for example by employing individuals in the state to sell its

products, produce its goods or perform services on its behalf to customers – state taxation and regulation is likely to be invoked.

⁷⁸ 120 F.3d 1006 (9th Cir. 1997) (en banc) cert. denied, 522 U.S. 1098 (1998); see also *Vizcaino v. United States District Court*, 173 F.3d 713 (9th Cir. 1999), amended by 184 F.3d 1070 (1999), cert. denied, 528 U.S. 1105 (2000).

⁷⁹ 141 F.3d 1405 (10th Cir. 1998).

⁸⁰ 26 U.S.C. § 882.

⁸¹ See 26 Code of Federal Regulations (“C.F.R.”) § 1.894-1.

⁸² See Canada – US Income Tax Convention, Article VII (1980).

VII. CONCLUSION

In a 2006 report on employee misclassification, the U.S. Government Accountability Office highlighted the many inconsistencies in classification standards and aptly observed that “the tests used to determine whether a worker is an independent contractor or an employee are complex, subjective, and differ from law to law.”⁸³ That observation remains true today. Indeed, not only do the tests vary, but so does their interpretation. Outcomes may vary from jurisdiction to jurisdiction and indeed from case to case. Navigating this legal maze can be challenging and treacherous. Any company doing business in the United States should tread with caution when hiring independent contractors and seek legal advice to manage the complexities of the legal landscape.

The use of independent contractors remains a viable and often a valuable means to supplement a company’s labor force. In light of increasing state and federal regulatory focus and ever-increasing class action activity, however, it is important that employers (particularly those in scrutinized industries) assess the applicable laws in their jurisdiction, implement lasting changes across their organization which accurately distinguish between employees and independent contractors, and (where independent contractors are used) document and structure independent contractor relationships in a compliant manner.

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⁸³ See *Donroy, Ltd. v. United States*, 301 F. 2d 200, 206 (9th Cir. 1962).



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