

Fair Work Ombudsman Inquiry Findings

The Fair Work Ombudsman's Inquiry into the Victorian
Department of State Development and Business Innovation-
labour hire and independent contractor arrangements

February 2015

Executive Summary

In November 2013, the Community and Public Sector Union SPSF Victorian Branch [CPSU] alleged the Victorian government's Department of State Development and Business Innovation [DSDBI] was involved in sham contracting.

The Fair Work Ombudsman's [FWO] Inquiry into whether the DSDBI's procurement of labour services contravened the 'sham contracting' provisions of the *Fair Work Act 2009* [FW Act] involved a detailed examination of key departmental policies, procedures, contractual documentation and interactions with senior DSDBI management, workers and union representatives.

The Inquiry found no evidence of sham contracting; however found that in seeking to achieve financial savings, the DSDBI had commenced experimenting with a changing operating model in 2013 characterised by heightened risk and an increasing use of non-traditional forms of labour engagement. In particular, the Inquiry found:

- the manner in which the DSDBI proposed to engage certain workers as independent contractors increased the risk of non-compliance with the FW Act;
- some workers may not be receiving their correct entitlements if they are characterised as independent contractors instead of more accurately classified as employees;
- a workforce reticent to complain publicly; and
- the DSDBI had not responded to or acted upon recommendations made by the Victorian Auditor-Generals' Office [VAGO] report concerning the procurement of labour.

On the basis of the Inquiry's findings, the FWO recommends:

- the DSDBI comprehensively review its labour engagement policies and processes, specifically, the recruitment of ongoing Victorian Public Service [VPS] employees, agency on-hire (labour hire) workers and independent contractors, to ensure compliance with the FW Act;
- the DSDBI self-audit the engagement of each of its independent contractors and any utilised through labour hire agencies who undertake work traditionally performed by VPS employees to ensure that each contractor is not more accurately classified as an employee;

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- the DSDBI ensure workers more appropriately engaged as employees receive their correct entitlements in accordance with the FW Act (this includes back payment of any outstanding entitlements which may be identified as owing to employees misclassified as independent contractors through DSDBI's self-audit);
 - that where the engagement of independent contractors has been proposed for various services traditionally performed by VPS employees, the DSDBI seek specific legal advice regarding the engagement of such independent contractors; and
 - the DSDBI note that the FWO will undertake further inquiries with the DSDBI within six months of this report to ascertain what action has been taken in response to the FWO's findings and to assess whether any potential misclassification has been addressed.

Background:

1. On 13 November 2013, the CPSU¹ met with officers from the FWO and alleged that the DSDBI was involved in sham contracting arrangements.
2. The CPSU alleged agency on-hire (labour hire) workers² had been presented with guidelines by certain DSDBI management representatives as to how to become independent contractors³ and how to obtain Australian Business Numbers [ABNs] so they could apply to work directly for the DSDBI rather than through labour hire agencies as employees.
3. The CPSU further alleged that the DSDBI employees had begun observing independent contractors working in positions that were traditionally performed by the DSDBI direct employees or agency on-hire workers.
4. The CPSU requested the FWO examine the practices engaged by the DSDBI in sourcing its labour requirements, in particular, concerns that 'core Victorian public

¹ The CPSU is a registered organisation comprised of two divisions – the Public Sector Union representing Commonwealth public sector employees and the State Public Services Federation (SPSF) representing state public sector employees in every state. The CPSU currently has approximately 140,000 members nationally. The allegations subject to this Inquiry were referred by the CPSU's SPSF Victorian Branch. For the purpose of this Inquiry report, reference to the CPSU is specific to the activities of the SPSF Victorian Branch.

² Agency on-hire workers are workers engaged through registered labour hire agencies to provide temporary workers to the DSDBI. The workers may be employees of the labour hire agencies or engaged as independent contractors by the labour hire agency. Agency on-hire workers are intended to back-fill absences of VPS employees who are either on short term approved leave, or in the case of longer periods, the position has been unable to be backfilled through local or advertised higher duties or advertised fixed term secondments.

³ An independent contractor is someone who is self-employed and provides services to clients, such as other businesses. An example of an independent contractor could be a plumber who is hired by a business to fix a burst pipe. The plumber attends the business with his own tools and employees, fixes the pipe, and then invoices the business for the cost of the job.

service' work was being outsourced to putative independent contractors in sham arrangements.

5. Upon the basis of documents provided to the FWO by the CPSU in support of its written allegations, the FWO agreed to conduct inquiries into the CPSU's allegations of non-compliance. Following receipt of additional evidence provided by the CPSU and the DSDBI, the FWO commenced a formal Inquiry on 16 December 2013.⁴
6. The purpose of this report is to provide the FWO's findings arising from the Inquiry into the procurement of labour by the DSDBI.

Who is the subject of this Inquiry?

7. The FWO's Inquiry involved the DSDBI; a department of the Victorian government created in April 2013⁵ comprising ten divisions that work together to support pro-business policies and programs, and the development of innovative industries for the state of Victoria.⁶ The divisions are:
 - (a) Chief Operating Officer
 - (b) Energy and Earth Resources
 - (c) Major Projects
 - (d) Trade, Manufacturing, Aviation and Employment
 - (e) Innovation, Services, Small Business and Technology
 - (f) Tourism and Airline Services
 - (g) Policy
 - (h) Corporate, Planning and Compliance Services
 - (i) Office of State Development, and
 - (j) Regional Development Victoria

⁴ On 23 January 2014, the CPSU posted an article on its website – www.cpsu.vic.org – titled '*Sham Contracting Under FWO Microscope*'. The article made reference to the FWO's Inquiry into the allegations raised by CPSU relating to potential contraventions of the *Fair Work Act 2009*.

⁵ Formerly the Department of Business and Innovation.

⁶ According to its website, the DSDBI's activities are designed, amongst other things, to generate job opportunities in Victoria www.dsdbi.vic.gov.au

Jurisdiction

8. The FW Act establishes Australia's national workplace relations system, which extends rights and obligations to employers, employees and others (notably independent contractors and registered organisations of employers and employees).
9. Under sub section 682(1)(c) of the FW Act, the FWO has the function of inquiring into, and investigating, any act or practice that may be contrary to the FW Act.
10. On the basis of the Victorian state government's referral of most of its industrial relations powers to the Commonwealth of Australia, the FWO has jurisdiction to conduct an Inquiry into the procurement of labour by the DSDBI.⁷
11. The FWO acknowledges it does not have jurisdiction to prescribe the number of workers who may be engaged in different capacities by the DSDBI (whether as VPS employees, agency on-hire (labour hire) workers or independent contractors), nor does the FWO seek to interfere with the DSDBI's discretion to outsource services. The purpose of the Inquiry is and was to assess whether the DSDBI's labour engagement practices comply with the FW Act.

What part of the FW Act has this Inquiry concentrated on?

12. The FW Act provides three 'sham arrangements' contraventions and these are contained in the General Protections provisions of the FW Act. They are:

Section 357 – Misrepresenting Employment as Independent Contracting;

Section 358 – Dismissing to Engage as Independent Contractor, and;

Section 359 – Misrepresentation to Engage as Independent Contractor

13. This Inquiry has primarily focussed on issues related to Section 357 - Misrepresenting Employment as Independent Contracting.

14. Subsection 357(1) of the FW Act relates to misrepresenting employment as an independent contracting arrangement and provides for the following:

*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.*

⁷ The DSDBI is a national system employer within the meaning of section 30D of the FW Act. Pursuant to the *Fair Work (Commonwealth Powers) Act 2009* (Vic), Victoria is a 'referring State' within the meaning of section 30B of the FW Act and the FW Act applies to most Victorian public sector employees.

15. However, a defence applies to a person (the employer) who has contravened subsection 357(1). Subsection 357(2) provides that subsection 357(1) does not apply where the employer proves that, when the representation (referred to in subsection 357(1)) was made, the employer:

(a) *did not know; and*

(b) *was not reckless as to whether;*

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

16. Knowingly or recklessly misrepresenting a contract of employment as a contract for services performed by an independent contractor is a contravention of subsection 357(1) of the FW Act, and can result in the imposition of penalties. The fact that a worker might prefer to be engaged as an independent contractor is not a defence to a 'sham arrangements' contravention under the FW Act.

17. Importantly, section 361 of the FW Act contains a reverse onus of proof for allegations falling within Part 3-1 of the FW Act which includes section 357.

18. A person or body found to be in contravention of a civil remedy within the FW Act is liable to a maximum penalty of up to \$10,200 for an individual and \$51,000 for a corporation, for each contravention.

How was the Inquiry conducted?

19. The FWO Inquiry was conducted by a careful examination of:

(a) The DSDBI's representations made to VPS employees and the general public regarding agency on-hire (labour hire) workers and independent contractors;

(b) the process by which independent contractors were engaged and whether the positions filled had been previously performed by employees;

(c) the activities that may have informed allegations of sham arrangements;

(d) whether there was any evidence that the DSDBI had engaged in sham arrangements;

(e) five examples of procurement for services through request for quotation [RFQ] and request for tender [RFT] processes; and

(f) whether the DSDBI had received legal advice prior to engaging independent contractors.

20. The Inquiry was conducted by Fair Work Inspectors [FWIs] appointed under section 700 of the FW Act and involved the following activities:

- (a) sourcing, reviewing and analysing information exchanged via telephone, email and meetings with CPSU officials, the DSDBI management representatives, and VPS employees;⁸
- (b) a review of the VAGO report on the 'Use of contract and temporary staff';⁹
- (c) examination of records and documents provided by the DSDBI and the CPSU, including information received from the DSDBI under the terms of a Voluntary Confidential Legal Professional Privilege Disclosure Agreement;
- (d) application of the 'multi-factor test' against various DSDBI RFQs, RFTs and positions held by external service providers. Refer to the '[Employees v contractors](#)' section for further information regarding the multi-factor test; and
- (e) reviewing submissions received from the CPSU and the DSDBI in regards to the FWO's preliminary findings arising from the Inquiry.

Sham Arrangements or Misclassification – Why does it matter?

21. According to the Australian Bureau of Statistics, there were 986,400 people who were independent contractors in their main job in November 2013.¹⁰ Independent contractors made up 8.5% of the working population. Of those, 28.3% worked in the state of Victoria. This represents a significant portion of the Australian workforce.

22. The FWO supports independent contractors operating businesses in the community by providing a series of tools and resources to help workplace participants understand how they, or those they engage for work, should be correctly classified. This in turn assists workplace participants to ensure entitlements, tax, insurance, workers' compensation, superannuation etc. are appropriately provided or obtained.

⁸ For the purposes of this Inquiry report, Victorian Public Service [VPS] employees refers to employees of the DSDBI only and does not represent the entire VPS. VPS employees are directly employed by the DSDBI and their working conditions are informed by the Victorian Public Service Workplace Determination 2012 [AG895510].

Fair Work Inspectors met with VPS employees who wished to remain confidential. Those employees requested confidentiality, with meetings held in the presence of a CPSU official. Details of the employees' designation were not provided to the FWO. FWIs also met with management representatives from the DSDBI.

⁹ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013.

¹⁰ Australian Bureau of Statistics, *Forms of Employment, Australia released on 7 May 2014* (cat. No. 6359.0).

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23. 'Sham contracting' occurs when an employer deliberately attempts to disguise an employee / employer relationship as an independent contracting relationship. 'Misclassification' occurs when an employer engages a worker as an independent contractor who is at law an employee but there is no evidence the engagement involved any deliberate intent to circumvent the existence of an employment relationship.¹¹
 24. Sham arrangements provide a business with an unfair competitive advantage against employers who are complying with their legal requirements.
 25. By disguising employment as independent contract work, employers avoid their obligation to provide employees with their correct entitlements such as minimum ordinary hour wages, overtime, penalties and other allowances. Employees may also have been denied access to leave payments, superannuation and tax exemptions.
 26. Contraventions of the sham arrangements provisions of the FW Act involve knowing or reckless behaviour designed to result in workers being denied employment benefits and protections. As stated, sham arrangements give the employer an unfair competitive advantage. Such contraventions are treated seriously and the FWO has instituted proceedings against several enterprises for engaging in this type of behaviour.¹²
 27. Misclassification of an employment relationship can result in a business being found to have contravened the National Employment Standards [NES], minimum wage orders, a Modern Award or an Enterprise Agreement as provided for in the FW Act.
 28. Although not deliberate, in some instances where there is misclassification of an employment relationship, employers are required to take corrective action and rectify underpayments resulting from any contravention.
 29. Misclassification and sham contracting can also result in contraventions of employer obligations to provide employee records and pay slips, and may expose employers to an infringement notice.¹³

¹¹ In November 2011, the FWO released its report into sham contracting and the misclassification of workers in the cleaning services, hair and beauty and call centre industries <http://www.fairwork.gov.au/Documents/Report-on-the-preliminary-outcomes-of-the-Fair-Work-Ombudsman-Sham-Contracting-Operational-Intervention.pdf>. The Report highlighted the need to use different language when describing contracted workers who are in fact employees but there is no evidence that such characterisation was either deliberate or reckless (referred to as '**misclassification**'), as opposed to intentional efforts to deny workers employment benefits by treating them as contractors (referred to as '**sham arrangement(s)**').

¹² On 26 July 2013, the Federal Circuit Court of Australia handed down its decision in the matter of *Fair Work Ombudsman v Happy Cabby Pty Ltd & Anor* (SYG1141/2012) ordering substantial penalties totalling **\$286,704** in respect of contraventions relating to sham contracting, underpayments, failure to make and keep employee records and failure to issue payslips.

¹³ As provided in s 558 (1) FW Act.

30. Where an employee / employer relationship is identified, the employer will also be required to ensure they met their legal obligations in relation to taxation and superannuation.

Employees v contractors

31. There is no single factor that, in isolation, can determine whether a worker should be more appropriately classified as an employee or an independent contractor. Rather, it is necessary to assess a number of factors concerning each specific engagement and consider the totality of the working relationship to determine whether a worker is, overall, more likely to be an employee or an independent contractor.

32. To distinguish between the two, the courts have established a number of characteristics of a working relationship that must be considered collectively to determine whether a relationship is more indicative of a contract of employment or a contract for services (i.e. an independent contracting relationship). This common law assessment is termed a 'multi-factor test'.¹⁴

33. In the course of its Inquiry, the FWO has applied the 'multi-factor test' to determine whether a worker should be treated as an employee or an independent contractor. This involved considering the totality of the situation and how the relationship operated on the ground on a day-to-day basis.

34. The key indicators that may contribute to determining whether a person is an employee or independent contractor include:

Indicator	Employee	Independent Contractor
Degree of control over how work is performed	Performs work, under the direction and control of their employer, on an ongoing basis.	Has a high level of control in how the work is done.
Hours of work	Generally works standard or set hours (note: a casual employee's hours may vary from week to week).	Under agreement, decides what hours to work to complete the specific task.
Expectation of work	Usually has an ongoing expectation of work (note: some employees may be engaged for a specific task or specific period).	Usually engaged for a specific task.

¹⁴ See for instance, A.Stewart, 'Stewart's Guide to Employment Law' 3rd edition (2011) Federation Press, Sydney.

Indicator	Employee	Independent Contractor
Risk	Bears no financial risk (this is the responsibility of their employer).	Bears the risk for making a profit or loss on each task. Usually bears responsibility and liability for poor work or injury sustained while performing the task. As such, contractors generally have their own insurance policy.
Superannuation	Entitled to have superannuation contributions paid into a nominated superannuation fund by their employer.	Pays their own superannuation (note: in some circumstances independent contractors may be entitled to be paid superannuation contributions).
Tools and equipment	Tools and equipment are generally provided by the employer, or a tool allowance is provided.	Uses their own tools and equipment (note: alternative arrangements may be made within a contract for services).
Tax	Has income tax deducted by their employer.	Pays their own tax and GST to the Australian Taxation Office.
Method of payment	Paid regularly (for example, weekly/fortnightly/monthly).	Has obtained an ABN and submits an invoice for work completed or is paid at the end of the contract or project.
Leave	Entitled to receive paid leave (for example, annual leave, personal/carers' leave, long service leave) or receive a loading in lieu of leave entitlements in the case of casual employees.	Does not receive paid leave.

Statement of key findings

35. Following a careful consideration of all the evidence, specifically, an examination of five of the DSDBI's procurement processes, the FWO makes the following findings derived from this Inquiry.

36. While the Inquiry found no evidence of 'sham contracting', of the five cases examined, two were considered likely to be lawful contracting arrangements and three were identified as raising concerns for the potential of misclassification of employees.¹⁵

37. The Inquiry noted that VPS employees were fearful of reporting their concerns to the FWO, except on a strictly confidential basis. VPS employees who confidentially met with

¹⁵ Three of the five cases studies examined have been summarised in this report. Those three case studies were also contained in the FWO's Statement of Preliminary Findings which the parties were invited to and did respond to.

the FWO expressed concern regarding the use of labour hire and independent contractors to undertake work traditionally performed by VPS employees.

38. The Inquiry found a connection between various State Budget Announcements dating back to 2011 and the DSDBI's labour procurement practices in 2013. In particular, in seeking to achieve savings required by the various budget announcements, the DSDBI had commenced changing operating model characterised by non-traditional forms of labour engagement.

State Budget Announcements – Victorian Public Service

On 15 December 2011, the then Treasurer of the State of Victoria announced the ‘Sustainable Government Initiative’ (SGI) comprising a number of ‘efficiency and revenue’¹⁶ measures to save \$3.1 billion over four years, following a review by Victoria’s Independent Review of State Finances finding that ‘growth in government expenses significantly outpaced revenue growth over the [preceding] decade’.¹⁷

Among the measures was a commitment to reduce the number of public servants in ‘non-service delivery and back-office roles’, with the Treasurer announcing that ‘VPS positions will reduce by about 3600 compared to current levels’.¹⁸ On 1 May 2012, a further reduction of 600 public service positions was announced as part of the Victorian Government’s 2012-13 Budget.¹⁹

On 22 June 2012, the former Premier of Victoria, the Hon Ted Baillieu, announced that the SGI reduction of 3,600 VPS employees would be achieved over two years through ‘natural attrition, a freeze on recruitment, the lapsing of fixed term contracts and Voluntary Departure Packages (VDP)’, with the reductions not applying to ‘frontline service delivery roles’ or exempt ‘specialist support staff’.²⁰

In the same statement, Premier Baillieu confirmed that as at 22 June 2012:

- ‘VPS numbers [had] already been reduced by 910 through [natural] attrition and non-renewal of fixed term contracts since December [2011];
- Applications [had] been made to the Australian Taxation Office for 2,600 VDPs across government departments and agencies;
- Departmental secretaries would be informing their staff about their department’s allocation of the 3,600 SGI headcount reductions’.²¹

In the two years ending 30 June 2013, the number of full-time equivalent (FTE) VPS employees decreased by 4,233 to 32,629 FTE employees.²²

On 13 December 2013, the Victorian Government claimed in its 2013-14 Budget Update that it has ‘driven public sector productivity by reducing back office costs ... and ... internal red tape’, and that the Labour Sustainability Cap would be introduced ‘to ensure the efficiency gains achieved through the SGI are not lost’.²³ The cap is intended to ‘moderate overall labour cost growth while providing flexibility to departments and agencies to deliver government business and service delivery needs’.²⁴

Victorian Government departments faced further budgetary and staffing restrictions from 1 January 2014, with the Victorian Government introducing a Labour Sustainability Cap which would ‘limit department and agency expenditure on VPS staff and contractors’.²⁵

¹⁶ 2011-12 Budget Update presented by The Hon. Kim Wells MP, Treasurer of the State of Victoria, Chapter 1 – Economic and fiscal overview, ‘Efficiency and revenue measures’ – page 5.

¹⁷ 2011-12 Budget Update, Chapter 1 - Response to the Independent Review of State Finances, page 4.

¹⁸ 2011-12 Budget Update presented by The Hon. Kim Wells MP, Treasurer of the State of Victoria, Chapter 1 – Economic and fiscal overview.

¹⁹ Media Release from the Premier on 1 May 2012

http://budget.vic.gov.au/domino/Web_Notes/budgets/budget12.nsf/d6e571e551bef80eca2572bb002bcea7/182c7e7024c52c45ca2579f10014328f!OpenDocument

²⁰ Statement issued by The Hon. Ted Baillieu MP Premier on 22 June 2012, titled “Sustainable Government Initiative Update”.

²¹ Statement issued by The Hon. Ted Baillieu MP Premier on 22 June 2012, titled “Sustainable Government Initiative Update”.

²² The State of the Public Sector in Victoria 2012-2013, page 83, Appendix B: The public sector workforce – in detail.

²³ 2013-14 Budget Update presented by The Hon. Michael O’Brien MP, Treasurer of the State of Victoria, Chapter 1 – Economic and fiscal overview, page 4.

²⁴ 2013-14 Budget Update presented by The Hon. Michael O’Brien MP, Treasurer of the State of Victoria, Chapter 1 – Economic and fiscal overview, page 4.

²⁵ 2013-14 Budget Update presented by The Hon. Michael O’Brien MP, Treasurer of the State of Victoria, Chapter 1 – Economic and fiscal overview, page 4.

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39. As at 30 June 2013, the DSDBI engaged 991 full time equivalent (FTE) VPS employees²⁶ and 277 employees²⁷ through a agency on-hire (labour hire) arrangement. At that time, almost 30 per cent of the agency on-hire (labour hire) workers had been engaged in that capacity for more than one year.²⁸ It is unknown how many workers had been engaged as independent contractors.
40. The number of agency on-hire (labour hire) workers, engaged through seven labour hire firms as per a whole of Victorian Government procurement panel arrangement, had increased from the 'historical' level of 100 to 200 agency on-hire (labour hire) workers.²⁹
41. The Inquiry disclosed this increase was due to recruitment freezes the DSDBI imposed internally, which were in addition to the Government's SGI, and which saw a reduction of about 100 FTE [DSDBI employees] as well as associated funding.³⁰
42. On 26 August 2013, in an all-staff email announcement, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI, advised that the DSDBI would be limiting its use of agency on-hire (labour hire) workers³¹ to temporary staffing to fill short-term absences or where a role could not be backfilled through higher duties or a fixed-term secondment.³²
43. In the same 26 August 2013 'all staff' announcement, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI stated that:
- *'all other service needs must be procured as services (not staffing) through competitive open market requests for quotations from commercial providers (registered businesses or companies)';*³³
 - whilst they would be *'confining'* of the use of on-hire workers, the agency on-hire (labour hire) workers' contracts would *'continue to be honoured until their completion'* and, with *'many ... due to expire before 4 October 2013'*, the

²⁶ The State of the Public Sector in Victoria 2012-2013, page 69, Appendix A: Employing organisations in the Victorian Public Sector.

²⁷ 277 temporary staff, Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 29, Figure 4D.

²⁸ 80 of 277 temporary staff equates to 28.9%, Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 29, Figure 4D.

²⁹ Information contained in an email from the DSDBI to the FWO dated 18 November 2013.

³⁰ Information contained in an email from the DSDBI to the FWO dated 18 November 2013.

³¹ From the mandatory [Victorian Government Purchasing Board] Staffing Services Panel.

³² DSDBI email entitled 'ALL STAFF: Accessing on-hire workers', DSDBI Staff Announcements dated 26 August 2013.

³³ DSDBI email entitled 'ALL STAFF: Accessing on-hire workers', DSDBI Staff Announcements dated 26 August 2013.

expiry of the contracts would *'now be staggered up to 1 November 2013'* due to *'the number involved'* with *'transitional arrangements'* to be established to manage the cessation of those contracts.³⁴

- DSDBI employees were prohibited from providing agency on-hire (labour hire) workers with support or assistance in relation to the procurement of services, including providing *'no advice (written or verbal)'*, *'coaching'* or *'solicitation'*.³⁵

44. In a letter to the CPSU dated 12 September 2013, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI, confirmed the impetus for reducing the number of agency on-hire (labour hire) workers was to generate cost savings:

*We expect that full commercial and competitive procurement of some functions presently undertaken by agency on-hire workers should deliver savings in both direct costs and agency commissions, thereby freeing up funds which could enable our ability to engage VPS staff.*³⁶

45. On 12 September 2013, DSDBI Deputy Secretaries were advised in an email by the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI, that following a review of requirements, agency on-hire (labour hire) workers could continue to be accessed for *'Executive Assistant / Personal Assistant Services'* and *'services that are substantially administrative support'* roles.³⁷

46. In the same 12 September 2013 email to Deputy Secretaries, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI, also stated in relation to the DSDBI's intention to replace agency on-hire (labour hire) workers with contract for services personnel, that:

We intend to be in the market for selected services in the next two weeks. Critically, one of those services will be business development services which are intended to be procured on a state-wide basis under a RFT process.

...

³⁴ DSDBI email entitled 'ALL STAFF: Accessing on-hire workers', DSDBI Staff Announcements dated 26 August 2013.

³⁵ DSDBI email entitled 'ALL STAFF: Accessing on-hire workers', DSDBI Staff Announcements dated 26 August 2013.

³⁶ DSDBI letter in reply to the CPSU, dated 12 Sep 13.

³⁷ DSDBI email entitled 'An update on the introduction of revised arrangements for the procurement of services', sent to all Deputy Secretaries (and Chief Operating Officer) on 12 September 2013.

*To accommodate the time needed to conduct these procurements, existing agency on-hire arrangements can be extended to 1 November 2013.*³⁸

47. The DSDBI submitted that procurement from the open market was restricted to *'the delivery of specified services'*, that the advertisements did not specify the number of people or hours required to perform the service and that *'generally, bidders can sub-contract, deliver services from their own locations and provide [their] own tools and equipment'*.³⁹

Case Study 1 - Events Management

In September 2013, the DSDBI released two separate requests for quotation (RFQs) in relation to the 2013 Trade Mission to China. The work involved facilitating events in China which included separate Expos in Shanghai and Tianjin.

The successful bidder was required to operate independently and 'carry out all arrangements' to facilitate the events, using their own resources, skills and expertise. The contract required the successful applicant to facilitate defined events during the limited period of the contract. This was not an ongoing business proposition and ended soon after the Trade Mission ended.

The FWO formed a view that by clearly defining the requirements, limiting the period that the work was to be undertaken in and allowing the successful applicant autonomy to deliver on the contract, that the relationship between the DSDBI and the successful applicant was one of a lawful independent contracting arrangement.

48. In a letter to the CPSU dated 22 October 2013, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI stated that *'these [new] commercial arrangements do not impact VPS positions'*, namely, they were aimed at replacing the use of agency on-hire (labour hire) workers.

³⁸ DSDBI email entitled 'An update on the introduction of revised arrangements for the procurement of services', sent to all Deputy Secretaries (and Chief Operating Officer) on 12 September 2013.

³⁹ Information contained in an email from the DSDBI to the FWO dated 18 November 2013.

Case Study 2 - Contact Call Centre Employees

In November 2013, in an effort to reduce the number of workers engaged through the DSDBI's panel of on-hire agencies, the DSDBI issued a request for quotation (RFQ) for contact call centre workers for Business Victoria. The contact call centre was already operational before the DSDBI sought labour through an RFQ for a provider to answer phone calls, emails and web chat enquiries.

One of the successful bidders was a labour hire company which, in their quotation, promoted their relevant experience on the basis of being able to provide a suitable individual who already worked at the DSDBI contact call centre.⁴⁰ We'll refer to the individual as Margaret.

Margaret had worked for the contact call centre for a year and a half through one of the DSDBI's existing labour hire agencies. The successful bidder nominated the DSDBI contact centre leadership personnel as referees to comment on Margaret's knowledge and experience.

Margaret essentially returned to her same job. However, she had now entered into a contract with a new company.

The FWO formed the view that the procurement exercise, which was open to individual suppliers as well as companies,⁴¹ raised the potential for misclassification.

49. On 27 November 2013, the VAGO Report regarding the 'Use of contract and temporary staff'⁴² was tabled in the Victorian parliament. The VAGO had examined the use of 'contract' and 'temporary' (on-hire) staff across 11 of Victoria's portfolio departments⁴³ during 2012-13 and concluded that the extended periods of engagement for those staff suggests that *'these resources were being used to fill permanent roles'*.

50. To consistently analyse the engagement practices for workers across the departments who are not *'permanent or ongoing staff'*, the VAGO Report provided a definition for a number of categories of worker engagement that may be used to *'deliver services to the public and generate economic benefit'*, including *'contract staff'*, *'temporary staff'* and

⁴⁰ The DSDBI submitted in correspondence to the FWO dated 30 September 2014 that 'Margaret' was an agency on-hire worker and an employee of the relevant labour hire company. The DSDBI further submitted that Margaret *'chose to resign... and take up employment with the successful bidder under the request for quotation process'*. In a meeting with the FWO on 23 September 2014, the DSDBI stated that it has 'effectively outsourced' the work.

⁴¹ On 28 November 2013, the DSDBI submitted to the FWO two template contracts for services, one for companies and one for individuals.

⁴² Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013.

⁴³ 11 portfolio departments include DSDBI; Education and Early Childhood Development; Environment and Primary Industries; Health; Human Services; Justice; Planning and Community Development; Premier and Cabinet; Primary Industries; Transport, Planning and Local Infrastructure; Treasury and Finance.

'consultants'.⁴⁴ The VAGO was 'unable to obtain complete and accurate information' regarding the use of contract staff across the portfolio departments due to 'the lack of data and centralised records' and, importantly, 'inconsistencies ... due to differing definitions used by portfolio departments'.⁴⁵

51. The VAGO cautioned the audited portfolio departments regarding their worker engagement practices stating that *'it is unclear whether individuals employed as contract staff for extended periods, are legally 'employees' entitled to accrue employee benefits'.⁴⁶*

52. The VAGO report expressed concerns that workers may not be appropriately engaged as employees and, therefore, not receiving their necessary statutory entitlements. These concerns were raised with direct reference to the requirements of the FW Act not to misrepresent employment as independent contracting. The VAGO stated the following in its report:

[Some contract staff] had become akin to members of portfolio departments staff rather than contract staff. This suggests that contract staff are being used to replace employees, rather than for specific purposes.

[In two previous VAGO reports tabled in 2012, VAGO] raised the need for agencies to properly assess contract and employee relationships. Employees are entitled to benefits such as sick leave, long service leave and redundancy payments. Such benefits are not available to contract staff.

It is important for portfolio departments to ensure that individuals are appropriately remunerated and receive employment benefits commensurate with their employment status and that the appropriate taxation provisions are applied. The Fair Work Act 2009 (Commonwealth) provides for civil remedies where an employer misrepresents employment as independent contracting.⁴⁷

53. To address the ambiguity regarding the differences between the various categories of worker engagement and to ensure employees are correctly engaged and remunerated, the VAGO made a number of recommendations, specifically including the need for

⁴⁴ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 21.

⁴⁵ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 21.

⁴⁶ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 21.

⁴⁷ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 21.

portfolio agencies to review their engagement practices and ensure individual workers are appropriately engaged:

All portfolio departments should have policies for engaging contract and temporary staff, and include a clear definition for each.

Portfolio departments should obtain legal advice on whether individuals employed over long periods are legally contract staff or employees and address any financial consequences.⁴⁸

54. All audited portfolio departments had an opportunity to respond to the VAGO report. The Inquiry disclosed the DSDBI did not provide the VAGO with a response to the report or its recommendations. The Inquiry considered this failure to respond as unusual, given the DSDBI's declared strategic intent to decrease reliance upon labour sourced from on-hire (labour hire) agencies and *'pursue innovation and value as it sees fit'*, including *'engaging consultants and others conducting their own business.'*⁴⁹
55. The Inquiry disclosed that the DSDBI had sought legal advice prior to the offering of contracts for service and / or procurement of services through market requests for quotations that are the subject of the FWO's current Inquiry.⁵⁰ The FWO obtained legal advice sought by the DSDBI through a 'Voluntary Confidential Legal Professional Privilege Disclosure Agreement'.
56. On 17 December 2013, the FWO met with the DSDBI's Deputy Secretary of Corporate, Planning and Compliance Services to discuss the DSDBI's engagement practices. At the meeting, the Deputy Secretary of Corporate, Planning and Compliance Services submitted he was not aware whether the DSDBI had criteria to determine whether to offer employment in a particular fact situation or indeed whether the DSDBI had a recruitment and selection policy.
57. At that meeting, however, the Deputy Secretary of Corporate, Planning and Compliance Services, DSDBI, disclosed a document titled 'RFQ Specifications – Consultancies /

⁴⁸ Part 4 of the Victorian Auditor-General's Report, Portfolio Departments and Associated Entities: Results of the 2012-13 Audits, November 2013, page 30.

⁴⁹ Quotations sourced from DSDBI's submission to the FWO in response to its preliminary findings, the DSDBI submission is dated 30 September 2014.

⁵⁰ During a telephone conversation of 14 November 2013, DSDBI's Deputy Secretary of Corporate, Planning and Compliance Services disclosed to the FWO's Executive Director – Dispute Resolution and Compliance that the DSDBI obtained legal advice prior to the offering of contracts for service and / or procurement of services through market requests for quotations that are the subject of the FWO's current Inquiry. As a result, the FWO offered, and the DSDBI accepted, the opportunity for the DSDBI to voluntarily provide the legal advice in a manner which maintained privilege. In accordance with the terms of the Voluntary Confidential Legal Professional Privilege Disclosure Agreement entered into on 17 January 2014, the FWO accepted the legal advice on a confidential basis. While the FWO may use the advice for the purposes of this Inquiry, it is not to disclose the information contained in the advice.

Independent Contractors / Companies' which had allegedly been circulated to the DSDBI officers responsible for the procurement of services. The document directs, in part, that:

- *Bidders should only be referred to as Service Providers or Suppliers*
- *The service specification in the RFQ should requires (sic) clear, measurable deliverables and where possible quantities ...*
- *Methodology should be completed only by the potential supplier. This, along with price, is the distinguishing competitive feature of bids. ...*
- *The supplier should only report to a nominated Contract Manager on a predetermined frequency. ...*
- *The proposed price of the supplier should be fixed. ...*
- *We should only accept proposed payment plans that are milestone based...⁵¹*

(No emphasis added)

Case Study 3 – Policy Writers

In September 2013, Regional Development Victoria (RDV) issued a request for quotation (RFQ) calling for professional writing and communication services for its Regional and Rural Policy Development project.

The work involved providing policy research and preparing new policies that would allow the Victorian Government to achieve growth in regional and rural Victoria.

There are a number of aspects of the engagement which are more indicative of independent contracting. These include the engagement being for a short period with payment made based on the achievement of pre-determined milestones.

However, another element which may be indicative of employment is the level of control DSDBI may have had over the successful bidder.

Policy writing is commonly performed by employees who have an in depth knowledge of the operations of government and policy requirements.

Closer scrutiny of the level of control exercised over the successful bidder would be required to satisfy the FWO that this is a legitimate independent contracting arrangement. The nature of the work does raise concern for the potential misclassification of employees.⁵²

⁵¹ DSDBI document titled 'RFQ Specifications – Consultancies / Independent Contractors / Companies', provided to the FWO on 17 December 2013.

⁵² The DSDBI's RFQ called for the 'provision of policy writing and development services for a Regional and Rural policy development project within Regional Development Victoria'. The RFQ summarised the purpose of the engagement as to provide 'policy research services including stakeholder engagement, professional writing services, co-ordination of artefacts and engagement schedules and communication programs'. In correspondence to the FWO of 30 September 2014, the DSDBI submitted that the FWO 'incorrectly, but understandably' referred to the suppliers as policy writers and that the nature of the work called for was 'broad

58. On 22 January 2014, the Inquiry disclosed that the DSDBI does have 'Recruitment Approval Guidelines'; however, the Guidelines do not provide a definition of independent contractors or how they differ from DSDBI employees or agency on-hire (labour hire) workers. Instead, the Guidelines simply state that *'hiring managers looking to engage a consultant or contractor must follow the Department's procurement of goods and services process'*.⁵³

59. The Inquiry disclosed no evidence of any further practical guidance to DSDBI management / recruiting staff regarding what is more typical of a contract for services (i.e. an independent contracting arrangement) than for a contract of employment.

Concluding observations

60. While the Inquiry found no evidence of 'sham contracting', there exists concern for the potential misclassification of employees.

61. The Inquiry concluded that the fissuring of the DSDBI's workforce in response to budgetary constraints risks non-compliance with the FW Act and potentially other legislation.

Recommendations:

62. The Inquiry expects that the DSDBI, as a large employer with a high degree of sophistication and available resources, will take the necessary action to reduce its risk of non-compliance with the FW Act.

63. On the basis of the Inquiry's findings, the FWO recommends that:

1. The DSDBI comprehensively review its labour engagement policies and processes, specifically, the recruitment of ongoing VPS employees, agency on-hire (labour hire) workers and independent contractors, so as to ensure compliance with the FW Act;
2. The DSDBI audit the engagement of each of its independent contractors and any utilised through labour hire agencies who undertake work traditionally performed by VPS employees to ensure that each independent contractor is not more accurately classified as an employee;

research and communications services'. The DSDBI submitted that it is incorrect to state that there would be some question as to the true independence of a supplier undertaking the work called for. As the FWO notes above, while the nature of the work does raise concern, the true nature of the engagement could only be determined with a closer assessment of how the supplier interacted with the DSDBI in practice.

⁵³ Information contained in an email from the DSDBI to the FWO dated 22 January 2014.

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3. The DSDBI ensure workers more appropriately engaged as employees receive their correct entitlements in accordance with the FW Act (this includes back payment of any outstanding entitlements which may be identified through the DSDBI's self-audit);
 4. Where the engagement of independent contractors has been proposed for various services traditionally performed by VPS employees, the DSDBI seek specific legal advice regarding the engagement of such independent contractors;
and
 5. The DSDBI note the FWO will undertake further inquiries with the DSDBI within six months of the report to ascertain what action has been taken in response to the FWO's findings and to assess whether any potential misclassification has been addressed.

Steven Ronson
Executive Director – Dispute Resolution and Compliance
Fair Work Ombudsman

February 2015

About the Fair Work Ombudsman

The Fair Work Ombudsman is an independent statutory agency, created by the *Fair Work Act 2009* (the FW Act) on 1 July 2009.

The Fair Work Ombudsman supports compliant, productive and inclusive Australian workplaces. We ensure compliance with Australia's workplace laws by:

- offering people a single point of contact to receive accurate and timely advice and information about Australia's workplace relations system;
- educating people working in Australia about their workplace rights and obligations;
- monitoring compliance with, inquiring into and, investigating any act or practice that may be contrary to workplace laws, awards and agreements; and
- litigating to enforce workplace laws and to deter people from not complying with their workplace responsibilities.

For further information and media enquiries please contact FWO media (media@fwo.gov.au).

If you would like further information about the Fair Work Ombudsman's compliance and enforcement activities please contact Steven Ronson, Executive Director – Dispute Resolution and Compliance (steven.ronson@fwo.gov.au).

A report by the Fair Work Ombudsman under the *Fair Work Act 2009*
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