

BREAKFAST SEMINAR SERIES

DID WE REALLY EMPLOY YOU?

Determining Independent Contractor Relationships

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Overview

- Types of relationships
- Common law tests
- Statutory tests
- Pitfalls to avoid
- How to create a “contract for services”
- Implications in an employer-employee relationship versus an independent contractor relationship
- Recent cases

The Independent Contractor

- Business trends in the past decade have created a body of self-employed workers known as independent contractors
- Reasons for choosing an independent contractor relationship
 - Workers
 - Employers

Definitions

- Employee
 - Contract of service
- Independent contractor
 - Contract for service

Employee or Independent Contractor? **How to determine it**

- Very difficult
- Parties' own definition of the relationship is not the deciding factor. The substance and the form matter
- A court or tribunal will look beyond the way the parties have described themselves

The Common Law Tests for Employment Status

- **Control Test**
- **Fourfold Test**
- Organization/Dependency/Integration Test
- Specified Results Test
- **Factors Approach**

The Control Test

- Measured by four factors:
 1. Employer's power over the selection of the employee
 2. Payment of wages and other remuneration
 3. Employer's right to control the method of doing the work
 4. Employer's right to suspend or dismiss the employee

The Fourfold Test

- “Whose business is it?”
- Four Factors:
 1. Control
 2. Ownership of Tools
 3. Chance of profit
 4. Risk of loss

The Combining Factors Approach

- Most widely used
- Affirmed by the Supreme Court in *Sagaz* (2001)
- Will apply all or some of the factors from the common law tests depending on the facts of the case
- Will try to determine the “full relationship” between the parties

The Combining Factors Approach

- Control
- Contractual language and intention of the parties
- Payroll practices
- Exclusivity
- Permanence and integration
- Risk and profit

Legal Consequences

When an independent contractor is found to be an employee

- Mischaracterization has grave legal penalties
- Different consequences under different legislation
- Requires an employer to fulfill their obligations
- Can attract large fines
- A finding under one piece of legislation may not result in a finding under another piece of legislation

Significance of a Determination

Legislative overview

- *Income Tax Act*
- *Employment Insurance Act and Canada Pension Plan*
- *Employment Standards Act*
- *Workplace Safety and Insurance Act*
- *Occupational Health and Safety Act*
- *Employer Health Tax Act*
- *Labour Relations Act*
- Common law
- Various Tribunals have additional guidelines and tests to determine whether a worker is an independent contractor

Income Tax Act

Obligations under the Act:

- The employer is required to deduct and remit income tax
- Finding will occur during an audit

Income Tax Act

Consequences:

- Offence for not withholding tax
 - Fine of not less than \$1000 and not more than \$25,000
 - Imprisonment of up to twelve months
- Penalty for failing to withhold
 - 10% of the amount that should have been deducted if done unknowingly
 - 20% of the amount that should have been deducted if done knowingly

Employment Insurance Act, Canada Pension Plan

Obligations under the Act:

- Deduct and remit EI premiums for employees
- Deduct and remit CPP contributions for employees
- Not required to deduct and remit for an independent contractor
- Allows actions against directors
- Finding will most likely occur if the independent contractor applies for Employment Insurance

Employment Insurance Act, Canada Pension Plan

Consequences:

- Liable for both employer and employee contributions
- Offence for a failure to deduct
 - Fine of not more than \$5000
 - Imprisonment of up to six months
- Penalty for failing to remit of 10-20% of the amount that should have been remitted

Employment Standards Act

Obligations under the Act:

- Minimum terms and conditions of employment respecting hours of work and eating periods, overtime, minimum wage, public holidays, leaves of absence, vacation with pay, and requirement to pay termination and severance
- Allows actions against directors

Employment Standards Act

Consequences:

- Order to pay
- Reinstatement
- Compensation
- Penalties for an offending individual
 - Fine up to \$50,000
 - Imprisonment of up to twelve months
- Penalties for an offending corporation
 - Fine up to \$100,000
 - Fine up to \$250,000 if corporation has a previous conviction
 - Fine up to \$500,000 if corporation has more than one previous conviction
- Fine for a director of up to \$50,000

Workplace Safety and Insurance Act

Obligations under the Act:

- Premium contributions per worker
- In the event of an accident, pay the worker for their full wages on the day of the accident
- Return to work obligations
- Experience-rated cost increases based on worker claim expenses for benefits, training, job search, etc.

Workplace Safety and Insurance Act

Consequences:

- Responsible for the claim and therefore higher costs
- Retroactively accrued premiums for the worker
- Audited by WSIB regarding all independent contractor arrangements
- Can be deemed responsible to pay premiums for those additional “workers”
- Possible fines for failure to report an accident

Occupational Health and Safety Act

- An employer must comply with the *Occupational Health and Safety Act* for an independent contractor as they do for employees

Employer Health Tax Act

Obligations under the Act:

- Remit premiums on total employee remuneration of over \$400,000 to contribute to Ontario's Health Care System
- Finding will occur during an audit

Employer Health Tax Act

Consequences:

- Repay premium
- Severe penalty based on return and number of months since premiums were due
- Offence for failing to deliver a return
 - Fine of not less than the greater of \$ 500 and 25% of the amount of tax and not more than double the amount of tax
 - Imprisonment of up to two years

Labour Relations Act

The Act:

- Allows employees to organize with unions
- Regulates the relationship between unions, employees and employers

Labour Relations Act

Consequences:

- Dependent contractors and employees are allowed to organize
- Independent contractor declared an employee and brought into the bargaining unit

Common Law – Wrongful Dismissal

Obligations under the law:

- Must provide reasonable notice to employees who are terminated without cause
- Factors considered:
 - Age
 - Position
 - Service
 - Availability of similar employment
- Occurs if the independent contractor files an action

Common Law – Wrongful Dismissal

Consequences:

- Reasonable notice
- Other damages

Pitfalls to Avoid

Termination and notice

- Employees
 - Entitled to reasonable notice based on *Bardal* factors
 - May be dismissed without notice for cause
- Independent contractors
 - Any ambiguity in a termination clause in a contract is likely to be interpreted in favour of the independent contractor
 - Termination provisions of the contract are interpreted literally
 - Notice must be given for contracts of indefinite duration

Pitfalls to Avoid **Intellectual property**

- Ownership of the product produced by the independent contractor can be difficult
- An independent contractor will almost always be the owner of any trade secret or patentable invention he or she invents and the owner of a copyright for any original works he or she creates
- If the employer wants the rights to any of these, they must indicate it in the contract at hire

Hiring an Independent Contractor

What you should ensure

- The individual has their own business and GST number
- If the individual requires assistance outside of the workplace, the individual hires that assistance
- The individual carries the financial risk of not completing their work
- The individual has clearance certificates from the WSIB

Designing the Contract

What should you include?

- No contract is completely safe
- Refer always to the individual as an independent contractor
- Clearly indicate that it is a contract for an independent contractor and not an employer-employee relationship
- Set out the services to be provided rather than list the position and duties
- Require invoicing rather than salary
- Include a time duration

Designing the Contract

What should you include?

- Include a termination provision and give at least 2 weeks notice of termination
- Include a provision which allows termination without notice for a fundamental breach
- Refrain from providing for strict supervision, have the independent contractor 'report'
- Refrain from having exclusivity clauses, allow the independent contractor to work elsewhere
- Ensure that there is a confidentiality clause
- Require the independent contractor to provide their own tools, supplies, inventory, equipment, and work space

Summary Checklist

- Employee:
 - Characterized as such in contract
 - Training is provided by company
 - Works on site
 - Company owns and supplies all tools and materials
 - Part of company benefits and pension plan
 - Corporation determines hours, pay scale
 - Paid on same schedule as other employees
 - Company makes statutory deductions (ie: tax, EI, CPP)
 - Company carries risk of financial loss
 - Worker is employed only by one company

Summary Checklist

- Independent Contractor:
 - Characterized as such in contract
 - Responsible for own training
 - Works off site or rents space from company
 - Worker owns and supplies own tools and materials
 - Manages own benefits and pension plan
 - Sets own hours and pay scale
 - Invoices company for work performed
 - Worker manages own income tax and insurance arrangements
 - Worker carries risk of financial loss
 - Worker has variety of clients

Recent Cases

Ambulance St-Jean v. Canada (F.C.J. – 2004)

- In determining if the individuals were employees or independent contractors, the Court relied on the intent of the parties when they contracted the relationship
- Intent should be given more weight, although it is not determinative

Recent Cases

Dynamex Canada Inc. v. Mamona (F.C.J. – 2003)

- Court deemed two independent contractors to be employees and allowed them to recover holiday pay and vacation pay
- Court stated that individuals may try to be independent contractors for the purpose of certain legislation and employees for the purpose of others
- This is correct in fact and law

Recent Cases

Aqwa v. Centennial Home Renovations (Ont. C.A. – 2003)

- Superior Court of Justice determined that the individual was an independent contractor but that the relationship was “akin to an employment relationship” and as such was entitled to reasonable notice despite clear, unambiguous termination clause
- Court of Appeal overturned the decision as there was no justification to make the changes