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***“Sale of Professional Services  
Businesses - Preserving Goodwill”***

Presented by  
Tom Meagher  
Director

# Tom Meagher | Director



**Tom has over 30 years' legal and business experience including:**

- **Being an owner and director of his former firm, Murfett Legal;**
- **Previously working for local law and major national firms;**
- **Being the national operations manager for a financial advisory IT platform provider;**
- **Previously being the WA Legal Technology Group Manager for a National Law Firm**
- **Owning and managing an IT consultancy business; and**
- **Being a director and in-house counsel for a public company.**

continued...

**Tom is also a regular published of articles and are Australia’s leading presenters of seminars to and for various professional bodies, associations and government authorities on a wide range of business law and professional development-training topics including:**

<b>WA Department of Commerce</b>	<b>Institute of Public Accountants</b>	<b>CPA Australia</b>
<b>Chartered Accountants Australia &amp; NZ (CAANZ)</b>	<b>Governance Institute of Australia</b>	<b>Mortgage &amp; Finance Association of Australia (MFAA)</b>
<b>Law Society of WA</b>	<b>National Electrical &amp; Communications Assoc (WA)</b>	<b>City Insolvency Discussion Group</b>
<b>Innovation Centre of WA</b>	<b>Australian Hotels Association (WA)</b>	<b>Forum for Directors of Indigenous Organisations (FDIO)</b>
<b>LegalWise CLE</b>	<b>Small Business Development Corporation</b>	<b>Stirling Business Centre</b>
<b>The Tax Institute</b>	<b>Australian Institute of Conveyancers (WA)</b>	<b>Institute of Certified Bookkeepers</b>
<b>Western Suburbs Business Association</b>	<b>Business Foundations Inc</b>	<b>WA Business Assist</b>
<b>WA Reckon Partners</b>	<b>WA Indian Docs Inc.</b>	<b>Australian Institute of Business Brokers (AIBB)</b>

# Overview

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# Who is an Employee and what is a Contractor?

- For many reasons, it is important for business to consider the legal nature of the workers they engage to carry out work for them
- Different classes of ‘worker’ face different treatment in differing contexts by legal and government authorities.
- The area of law concerning the divide between independent contractor and employee is not clear cut. (tip: ‘substance over form’).

# Commons Myths about the Employee/ Contractor Decision

(source: ATO)

- HAVING AN AUSTRALIAN BUSINESS NUMBER (ABN)
  - Myth: *if a worker has an ABN they are a contractor.*
- COMMON INDUSTRY PRACTICE
  - Myth: *everyone in my industry takes on workers as contractors, so my business should too.*
- SHORT-TERM WORK
  - Myth: *employees cannot be used for short jobs or to get extra work done during busy periods.*
- REGISTERED BUSINESS NAME
  - Myth: *if a worker has a registered business name they are a contractor.*
- CONTRACTING ON DIFFERENT JOBS
  - Myth: *if a worker is a contractor for one job, they will be a contractor for all jobs.*
- 80% RULE
  - Myth: *a worker cannot work more than 80% of their time for one business if they want to be considered a contractor.*



# Commons Myths about the Employee/ Contractor Decision

*(source: ATO)*

- PAST USE OF CONTRACTORS
  - Myth: *my business has always used contractors, so we do not need to check whether new works are employees or contractors.*
- PAYING SUPER
  - Myth: *my business should only take on contractors so we do not have to worry about super.*
- SPECIALIST SKILLS OR QUALIFICATIONS
  - Myth: *workers used for their specialist skills or qualifications should be engaged as contractors.*
- WORKER WANTS TO BE A CONTRACTOR
  - Myth: *my worker wants to be a contractor, so my business should take them on as a contractor.*
- USING INVOICES
  - Myth: *if a worker submits an invoice for their work, they are a contractor.*

# Distinguishing Characteristics of an Employee vs a Contractor

(source: ATO)

<u>Employee</u>	<u>Contractor</u>
An employee works in your business and is part of your business. Characteristics of an employee include the following.	A contractor is running their own business and provides services to your business. Characteristics of a contractor include the following.
<b>Ability to sub-contract/delegate:</b> the worker cannot sub-contract/delegate the work - they cannot pay someone else to do the work.	<b>Ability to sub-contract/delegate:</b> the worker is free to sub-contract/delegate the work - they can pay someone else to do the work.
<b>Basis of payment:</b> the worker is paid: <ul style="list-style-type: none"><li>• for the time worked</li><li>• a price per item or activity</li><li>• a commission.</li></ul>	<b>Basis of payment:</b> the worker is paid for a result achieved based on the quote they provided.



- Employee
- Independent Contractor

# Distinguishing Characteristics of an Employee vs a Contractor

(source: ATO)

<u>Employee</u>	<u>Contractor</u>
<p><b>Equipment, tools and other assets:</b></p> <p>your business provides all or most of the equipment, tools and other assets required to complete the work, or the worker provides all or most of the equipment, tools and other assets required to complete the work, but your business provides them with an allowance or reimburses them for the cost of the equipment, tools and other assets.</p>	<p><b>Equipment, tools and other assets:</b> the worker provides all or most of the equipment, tools and other assets required to complete the work. The worker does not receive an allowance or reimbursement for the cost of this equipment, tools and other assets.</p>
<p><b>Commercial risks:</b> the worker takes no commercial risks. Your business is legally responsible for the work performed by the worker and liable for the cost of rectifying any defect in the work.</p>	<p><b>Commercial risks:</b> the worker takes commercial risks, with the worker being legally responsible for their work and liable for the cost of rectifying any defect in their work.</p>
<p><b>Control over work:</b> your business has the right to direct the way in which the worker performs their work.</p>	<p><b>Control over work:</b> the worker has freedom in the way the work is done subject to the specific terms in any contract or agreement.</p>
<p><b>Independence:</b> the worker is not operating independently from your business. They work within and are considered part of your business.</p>	<p><b>Independence:</b> the worker is operating their own business independently from your business. The worker performs services as specified in their contract or agreement and is free to accept or refuse additional work.</p>

# Distinguishing Characteristics of an Employee vs a Contractor *(source: ATO)*

- Issues at stake:
  - Not just legal issues but significant tax, insurance and financial consequences can also adversely apply.
  - For instance, a principal will be liable for superannuation and workers' compensation for all employees but only for some independent contractors (who are classified as workers).
- Workers who are employees:
  - Some types of workers are always employees as they have all or most of the listed employee characteristics. Workers who are employees include:
    - apprentices
    - trainees
    - company directors.
    - Note also 'call centre operators' & cleaners



# Contractor – Types and Form

(can be an individual, partnership, company or trust)

## ***Sample Contractor Agreement***

- Subcontractor's Duties and Responsibilities
- Consideration
- Reporting
- Directions
- Completion of works
- Warranties
- Variations to the Works
- Performance
- Term
- Invoicing and payment
- Insurance
- Confidentiality and Intellectual Property
- Termination
- Force Majeure/ Act of God
- Sub-Contracts
- Conflicts of interest



- Statutory compliance
- Principal's instructions
- Maintenance of Works Site
- Relationship and Limited Agency
- No Competition
- Covenant not to solicit Principal's employees
- Access to records
- Indemnity
- Retention
- Liquidated Damages
- Dispute resolution
- Special conditions
- Miscellaneous

# “Alienation of Personal Services Income” (PSI)

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- The PSI legislation makes it clear that an entity or individual falling within the PSI rules would be limited to deductions available to an individual.
- Regarding the alienation of income, (apart from the existing general anti-avoidance tax provisions of Part IVA of the ITAA 36), there are no specific rules to address the adverse revenue implications which can result when alienation occurs.



- “PSI income” (whether ordinary or statutory income) is defined as that which is “gained mainly as a reward for the personal efforts or skills of an individual”.

# “Alienation of Personal Services Income” (PSI)

- Income that is gained by an entity (eg, a company, partnership or trust) for the personal efforts or skills of an individual will still be PSI. hence the ‘alienation’ aspect.
- By reason of this definition, income which is:
  - ancillary to an entity supplying goods or granting a right to use property; or
  - principally generated by assets an entity holds;
  - is not PSI, as it is not paid mainly as a reward for an individual’s personal effort.
- Rather, it is paid mainly as consideration for the provision of the goods or due to the use of an asset.

# “Alienation of Personal Services Income” (PSI)

- Generally, if a person or the personal services entity:
  - do not satisfy what is known as a "results test" (see below); and
  - that person or the personal services entity get 80% or more of the personal services income from one source,

then they will be subject to the PSI rules.
- The "results test" is satisfied where:
  1. *you work to produce a result, and*
  2. *you provide the tools and equipment necessary (if any) to produce the result, and*
  3. *you are liable for the cost of rectifying any defective work.*

# “Alienation of Personal Services Income” (PSI)

- The PSI rules are structured so that an individual or a personal services entity carries on a personal services business (and so is exempt from the rules) if:
  - A. the individual or, where the individual's PSI is included in a personal services entity's income, the entity meets the results test; or
  - B. not more than 80% of the individual's or entity's PSI in an income year comes from the one client (and associates of the client) and the individual or entity meets at least one of the unrelated clients test, employment test and business premises test; or
  - C. a personal services business (PSB) determination is in force. A PSB determination from the Tax Commissioner is necessary if the "80% threshold" and the results test are not met.

# “Alienation of Personal Services Income” (PSI)

- *Many small business operators, whether operating as individuals or through interposed entities, may find it difficult to pass the relevant tests to be regarded as carrying on a personal services business.*



# Employment Types

- *Casual*
- *Part-time*
- *Full time*
- *Fixed term*
- *Commission*
- *Contract*



- Casual employees are entitled typically to a casual loading under many awards but have no right to annual, sick and long service leave.
- However, if you engage casual staff on regular hours/days and/or times, for an on-going basis, those employees may become permanent part-time thereby entitling them to pro-rata paid leave.

# Recommended Provisions in an Employment Agreement

- Award (if applicable)
- Position
- Duties
- Lawful Directions
- Hours of duty
- Remuneration (and pay review)
- Probation
- Superannuation
- Annual and other leave
- (Sick, Carers, Bereavement, parental & Long Service)
- Intellectual property
- Confidentiality
- Other employment and conflicts of interest
- Personnel/operations Manual (and standards)
- Suspension
- Termination (and notice)
- Redundancies
- Employee Liability
- Dispute resolution
- Set-off (e.g. no leave loading and Award variation)
- Employee pays for any unused insurances, memberships and expenses
- Salary sacrifice
- Miscellaneous



# State or Federal Employer ?

*(source: WA Dept of Commerce)*



- The Western Australian state system covers employers who are not “constitutional corporations” and their employees.
- In general terms, this includes employers who are sole traders, and some partnership and trust arrangements.
- The Federal industrial relations system broadly covers employers who are “constitutional corporations” and their employees.

# State or Federal Employer cont'd ?

*(source: WA Dept of Commerce)*

- A constitutional corporation is incorporated. Incorporation can be done under:
  - the federal *Corporations Act 2001 (Cth)*; or
  - under other legislation, such as the *WA Associations Incorporation Act 1987 (WA)*.
- The constitutional corporation engages in trading or financial activities.
- There is no absolute rule that determines whether a particular corporation is covered by the national industrial relations system.

# State or Federal Employer ?

*(source: WA Dept of Commerce)*



- Broadly speaking, Proprietary Limited [Pty Ltd] or Limited [Ltd] companies tend to be in the national system by virtue of their trading or financial activities.
- Consider also:
  - Overseas Corporations
  - Partnerships; and
  - Trusts



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# State or Federal Employer cont'd?

*(source: WA Dept of Commerce)*

- Relevant Legislation
  - Modern Awards (State & Federal), National Employment Standards (NES) and Acts such as:
    - *Fair Work Act 2009 (Cth) or Industrial Relations Act 1979 (WA)*
    - *Minimum Conditions of Employment Act (1993)(WA)*
    - *Superannuation Guarantee (Administration) Act 1992 (Cth)*
    - *Income Tax Assessment Act 1997 (Cth) and the Taxation Administration Act 1953 (Cth);*
    - *Fringe Benefits Tax Act 1986 (Cth)*
    - *Public and Bank Holidays Act 1972 (WA)*
    - *Long Service Leave Act 1958 (WA).*

# State or Federal Employer cont'd?

*(source: WA Dept of Commerce)*

- Enterprise Bargaining Agreements (EBAs), Individual Flexibility Arrangements (IFAs) & varying awards (the “better off overall” test)
- Required Federal Employment documents: *Fair Work Act Information Statements* and payslips.
- Note for ‘high income earners’ (currently \$148,700 per annum and indexed annually), a Modern Award will not apply, but the NES will.

# Commission Based Employment

*(Real Estate Agents)*

- Under the Real Estate Industry Award 2010 (MA000106) (“Award”), commission-only arrangements are applicable only when if it can be demonstrated that an employee has:
  - earned more than the minimum wage payable under the Award
  - selling real estate in any 12-month period,
  - over the preceding 5 years.
- Minimum requirements:
  - Employee agrees in writing with the employer to be remunerated on a commission-only basis and how it is calculated
  - The employee is at least 21 years of age



# Commission-Based Employment cont'd

- The employee is not engaged as a casual, a junior, a property sales associate or a trainee; and
- The employee can demonstrate (with the present or any past Employer) that they have achieved the minimum income threshold in accordance with the minimum weekly wages as specified by the Award (see clause 16.3(a)(i) and (ii)).



# Restraints of Trade and Protective Covenants

- A 'Restraint of Trade seeks to restrict the freedom of a person to trade, undertake their livelihood or deal in specified ways with assets, information or third parties.
- It can apply during a contractual relationship and also for a period after its termination or expiry.
- The law is that a restraint of trade is:
  - contrary to public policy; and
  - unenforceable,  
unless the restraint is *reasonable* in the parties' interests and also in the public interest.



# Restraints of Trade and Protective Covenants cont'd

- Must be reasonable in the context as to:
  - Scope;
  - Location; and
  - Durationcommonly drafted in 'cascading' form.



- Protective Covenants (i.e. restrictive promises) can be enforced, if clear and agreed e.g. not to 'solicit' (i.e. poach) clients/customers, other staff or suppliers of the principal.
- Note also 'no conflict of interest' clauses.

# Confidentiality & Intellectual Property

- Employer has the right confidentiality from employees.
- Consider also 'ownership' of mobile phone number and LinkedIn account.



- All IP created by an employee automatically belongs to their employer (tip: still good to expressly state such in their employment agreement).
- However any and all IP rights created by an contractor remains theirs, unless they *expressly* agree to transfer such to the principal (e.g. by way of the subcontractor agreement).

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# Policies, Standards & Procedures

- If you want to enforce them you must provide them to the employees and subcontractors (before they accept their agreement).
- Types of policies may include:
  - Occupational Health & Safety.
  - IT, Email and Social Media.
  - Drug & Alcohol.



# Sale of an Employer's Business

- ‘Transmission of business’ & deemed continuous employment of transferring employees
  - Note: to check carefully to determine ‘accrued liabilities’; especially if you’re told “they’re all casuals”.
  - Seek copies all current signed employment agreements, title/position, date of commencement , days/ hours of work, accrued leave entitlements and current rates of pay (check payroll data).
  - Note also transfer of “accrued liabilities amortization factor”. Usually 60- 70%.
- However for a Subcontractor’s Agreement either:
  - express provision/rights for assignment (i.e. transfer) of the agreement; or
  - otherwise by mutual consent.



# Insurances

- Types of Business Insurances may include:
  - Workers Compensation,
  - Business Interruption,
  - Professional Indemnity,
  - Public Liability,
  - Directors & Officers/Management Liability,
  - Cyber & Privacy Risks,
  - Corporate Travel,
  - Construction, Farm,
  - Product Liability,
  - Motor Fleets,
  - Marine Cargo etc.



# Worker's Compensation Insurance

*WorkCoverWA*

(source:   
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- Under the *Workers' Compensation and Injury Management Act*, an employer's obligations include:
  - having workers' compensation (including common law damages) insurance cover for all 'workers' (penalties apply for failing to do so);
  - providing the worker's completed claim form and medical certificates to your insurer within 5 working days;
  - making weekly payments to the injured worker as soon as the claim is accepted or an order or direction is made to do so from WorkCover WA's Conciliation and Arbitration Services. Thereafter, a worker is to be paid on their regular pay day;
  - having an injury management system; and
  - developing and implementing a return to work program if a treating medical practitioner indicates it is needed for an injured worker.



# Worker's Compensation Insurance cont'd

*(source: WorkCoverWA)*

## Covering your Workers

- You must provide workers' compensation for anyone you employ who the legislation defines as a 'worker', including cover for claims at common law.
- The definition of a 'worker' covers:
  - full-time workers on a wage or salary
  - part-time, casual and seasonal workers
  - workers on commission
  - piece workers
  - working directors
  - contractors and sub-contractors (in some circumstances)
  - family members.
- This definition is broad and can be broken up into two parts: 'primary' and 'extended'.



# Worker's Compensation Insurance cont'd

*(source: WorkCoverWA)*

## Primary Definition of a Worker

- This covers any person who works under a contract of service or apprenticeship with you. The contract may be expressed or implied, oral or written. A large part of the workforce is covered under this part of the 'worker' definition, including:
  - full-time and part-time workers
  - casual workers
  - seasonal and piece workers
  - workers on salary or wages
  - workers supervised and controlled by an employer
  - workers who may be fired by an employer
  - workers who work for only one employer
  - workers with set hours of work.

# Worker's Compensation Insurance cont'd

*(source: WorkCoverWA)*

## Extended Definition of a Worker

- This covers any person who works under a contract for service. Many people who work as contractors or sub-contractors may be covered under this part of the definition, and it may cover workers who:
  - are paid on piece rates, hourly rates or per job
  - work for the employer on a 'one-off' or per job basis
  - do not have set hours of work
  - work for more than one employer
  - work unsupervised
  - pay 20% prescribed payments (sub-contractor's tax)
  - are covered by an industrial award or agreement.



# Worker's Compensation Insurance cont'd



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*Failure to Insure - Directors may be Personally Liable*

- If there are 2 or more responsible officers they are jointly and severally liable.
- It is important to note that the WCIM Act specifically states that where a body corporate commits an offence if they fail to comply with section 160(1) or (2) or gives a false estimate or statement as to the currency of the Worker's Compensation Insurance, **every responsible officer commits the like offence!** (section 170(5) WCIM Act).



# OSH and Directors Liability

- As a director, there are circumstances in which they may bear **personal liability** for acts and omissions on the part of the company in relation to safety.
- Section 55(1) of the *Occupational Safety and Health Act 1984* (WA) (“**OSH Act**”) provides that company officers, managers and persons with delegated authority (**Directors**) face **personal criminal liability** for company safety breaches if the offence occurred with the consent, connivance or negligence of the Director.
- The scope of this duty extends to what the Director ought to know as well as his or her actual knowledge.



# OSH and Directors Liability cont'd

- The scope of this duty extends to what the Director ought to know as well as his or her actual knowledge.
- When operating outside the borders of Western Australia, the *Work Health and Safety Act 2011* (Cth) (“**WHS Act**”) imposes somewhat broader duties on corporations and directors. Foremost (although arguably the duty exists implicitly in the OSH Act), there is a duty of “due diligence” imposed on directors (and other persons).

# OSH and Directors Liability cont'd

- Section 27 of the WHS Act requires directors to show that they have taken reasonable steps to:
  - acquire and update their knowledge of health and safety matters;
  - ensure that the person conducting the business or undertaking (“**PCBU**”) has, and uses, appropriate resources and processes to eliminate or minimize health and safety risks arising from work being done;
  - ensure that the PCBU has appropriate processes in place to receive and respond promptly to information regarding incidents, hazards and risks;
  - ensure that the PCBU has, and uses, processes for complying with duties or obligations under the WHS Act.

# Worker's Compensation Insurance

*WorkCoverWA*

(source:  
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## Exclusions

- Generally, individual workers *cannot* cover themselves for workers' compensation, even if they are self-employed and have an ABN.
- An exception is when an individual is a working director of a company.



# Consequences and Penalties

- Various government authorities have extensive powers to conduct audits and prosecutions for breaches of obligations towards employees and workers.
- The **ATO** is aggressively prosecuting late BAS lodgement and payment and non-compliance with superannuation obligations.
  - PAYG withholding penalty for not meeting your PAYG withholding obligations



# Consequences and Penalties

## ATO Penalties Cont'd

- Super Guarantee Charge for not meeting your super obligations, made up of:
  - super guarantee shortfall amounts (amount of super contributions which should have been paid into a complying fund)
  - interest
  - an administration fee.
  
- Note: Unlike Super Guarantee Contributions, the Super Guarantee Charge is **not** deductible!



# Consequences and Penalties

- Equally, the **Fair Work Commission** conducts audits to ensure all federal entitlements ( e.g.e Fair Work Act and relevant Award, if applicable) are paid.
- **WorkCover** conducts random audits to ensure that all ‘workers’ are covered by workers’ compensation and the maximum fine is \$5,000 per worker per week of no insurance.



# Consequences and Penalties

**Office of State Revenue (OSR)**, conducts random audits for Payroll Tax liabilities.

- Payments to ‘contract workers’ will be taxable if an ‘employee/ employer relationship exists between the employer and the worker. Watch also for ‘grouping’ issues’.
- Again fines, in addition to Payroll Tax liabilities, will apply.
- (Tip: there is a 25 page ‘self assessment’ questionnaire and 19 Commissioner’s Ruling available on OSR’s website)



# Thank You!



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