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HIA Submission to the Inquiry into the Operation of Queensland's Workers Compensation Scheme – July 2012

Background

HIA represents a broad spectrum of businesses across the home building industry. Membership covers builders, contractors, manufacturers and suppliers of building materials and building industry professionals. HIA members are involved in all facets of the home building industry from minor domestic renovation work through to the construction of high rise apartment buildings. The majority of HIA's membership comprises small family-owned contracting businesses.

This submission focusses mainly on the Committee's first consideration: that is the performance of the workers compensation scheme in meeting the objective spelt out in the Act. HIA considers that the operation of the scheme is performing poorly in meeting the objective in Section 5 (5) of the Act namely:

> *"Because it is in the State's interests that industry remain locally, nationally and internationally competitive, it is intended that compulsory insurance against injury in employment**should not impose too heavy a burden on employers**(emphasis added) and the community."*

This submission explains how the operation of the scheme is placing an unacceptable burden on employers in the home building industry.

Home Building Not Well Suited to the Workers Compensation Legislative Environment

To reflect the highly volatile levels of activity in the home building industry and the specialised nature of its skills base, the home building industry has responded through the development of a contract-based system of delivery. Using this contract-based approach to home building has delivered Australia what is regularly regarded as one of the most efficient home building industries in the world.

But the contract system does not fit well into Queensland's workers compensation scheme.

The area where the home building industry's contractors have the most difficulty in navigating the workers compensation system is in the fundamental question of who should be covered by the scheme. The definition of "worker" for the purposes of workers compensation has evolved and broadened over recent years to the point where almost all home building contractors who were previously outside the application of workers compensation have been swept up into the worker definition by a series of tribunal decisions rather than any well considered and discussed legislative amendments.

Operating within this ever-changing and very grey administrative area around the definition of a worker is a major red tape issue for all operators in the home building industry.

Report from a HIA member conversation about workers compensation:

The member has expressed a worry that he will be driven out of the industry, and considers the determination of a contractor's status to be ***'the biggest headache'*** a small business in the construction industry has. He voiced concerns that contractors are determined from several different perspectives, and that industry needs ***'a single test'***.

The *Workers Compensation and Rehabilitation Act 2003*recognises that there are some forms of skills engagement that are not well suited to the legislative approach to determining who is a worker, but home building contractors are not covered by these exemptions. Schedule 2 to the Act provides exemptions from the scope of the worker definition for paid sportspeople, the crew of commercial fishing boats and driving instructors.

There are many people operating a home building contracting business who have their own employees yet are captured themselves within the definition of worker. HIA would argue that it was never the intention of the legislators to have the Act apply to such people who are genuinely in business.

Report from a Brisbane Concreting Contractor
This contractor member engages sub-contractors who are a business in their own right. Each of the sub-contractors has employees working for them, and/or engages other sub-sub-contractors. It is a requirement of the trade contract that each of these sub-contractors have all their own income protection, and public liability insurances. All of the sub-contractors are paid for a specific outcome. In all other jurisdictions these sub-contractors would be considered genuine sub-contractors, however given the nature of concreting work, the workers are considered 'substantially labour' only for the purposes of WorkCover. The member and contractors are at a loss as to why such contractors are considered 'workers'.

Business Risks from an Uncertain Worker Definition

For someone who is not an employee the main test of whether they are a worker or not is if their contract is for "substantially labour only". This has led to many and shifting interpretations of what is "substantially" and indeed what is "labour".

Over time "substantial" has come to be interpreted as more than half of a contract's value. But home building contractors do not quote for work on the basis of separating labour from materials or the supply of plant and equipment. This leaves whomever they are contracting to in a quandary about the potential for these contractors to be deemed to be workers should their judgement be tested by WorkCover.

Moreover the concept of "labour" has become vague with some interpretations making distinctions between labour and skill. Some building trades are regarded as having "skill" and are therefore not workers while other who may well have undertaken the same amount of training are regarded as supplying "labour" and are therefore deemed to be workers.

Gold Coast small sole trader business
Member engaged contractor for a period of a month and was audited by WorkCover as a result of the contractor injuring himself on site. The contractor was a qualified carpenter (also a sole trader) who signed a period trade contract, provided tools, and materials, being paid for a specific result. Upon becoming aware of the audit, the sub-contractor provided an affidavit to WorkCover as to his contracting status. The contractor in his own mind was a business in his own right, and wanted the freedom associated with a contracting arrangement. WorkCover determined the worker to be 'substantially labour only'. The member applied for a review of the decision of WorkCover via QCOMP, which was subsequently overturned. The inconsistent and uncertain application of such decisions between authorities makes it difficult for small businesses to ensure compliance, with unnecessary stress, and time out of work. The member has stated *'let's hope common sense prevails'* as a result of this WorkCover review.

The net result of these uncertainties surrounding who is a worker is that determinations can only be made on a case-by-case basis and most alarmingly for business, can only be made retrospectively. But the workers compensation system requires business to specify in advance when they submit their annual WorkCover returns which of their contractors are likely to be regarded as workers and how much they are going to pay those contractors for their labour. Not only do employers have to predict how frequently they will use a contractor they also have to predict whether each contract with that contractor will be "substantially" for labour only, whether the contractor will be incorporated and the nature of future contractual relationships. In an industry as volatile in its demand for skills as home building it is simply impossible for businesses to make such predictions about their contractors with any degree of accuracy.

The confusion over who is to be regarded as a worker becomes even more complex where the contracted part is a partnership. The Act states in Schedule 2 Part 2 section 1 that

> *"A person is not a worker if the person performs work under acontract of service with—*
>
> *(a) a corporation of which the person is a director; or*
>
> *(b) a trust of which the person is a trustee; or*
>
> *(c) a partnership of which the person is a member"*

Notwithstanding the provisions of clause (c) WorkCover have determined that if only one of the partners in the business is performing the core business of the enterprise then that person may be a worker. For example in the common husband and wife small business partnership, the husband tiler may be a worker because his wife does no tiling, even though she may be managing employees, invoicing, marketing and customer relations. As the quote below from an HIA member explains, this interpretation implies a whole extra level of inquiry by the contracting party in trying to resolve their contractor's worker status.

'(we) not only have to ask is someone a partnership but then also delve into their partnership arrangements and agreement perhaps and look closely at their personal business structure and then take a look at whether they are doing substantially labour only. Another prime example or red tape gone mad. There is no definitive test that a builder can say yes they are a partnership so don't have to worry'.

These risks that home building businesses are taking in trying to determine who is a worker and how much they might be paid for their labour are not insignificant. HIA members have had audits resulting in anything up to hundreds of thousands of dollars in back-payments of WorkCover premiums, while a few have also overpaid.

Worker Definition Not Consistent with Other Definitions

To further complicate the difficulties imposed on home building businesses by the confusion over who is a "worker" for workers compensation purposes, the definition is now substantially different from other definitions used by State and Federal Government agencies. At a State level for the building industry there are at least four different definitions used to make the distinction between contractors and workers by WorkCover, Q Leave, payroll tax, and the Building Services Authority.

HIA has recently made submissions to the Government recommending that these four agencies should align their definitions into one consistent approach. A copy of HIA's submission is at Attachment A.

A Transparent and Efficient Worker Definition

In this submission HIA urges the Government one predictable and simple to administer rule for determining who is a contractor that is based on the GST system. HIA contends that anyone who is registered for the GST system and who charges their client GST for their work is in business and should not be regarded as employees or workers.

HIA would argue that where an entity meets these criteria they have an intention to be in business rather than be an employee. Additionally the business engaging their services expects to be able to treat the entity as contracting business.

Critics may suggest that if this approach was adopted employers would compel workers to register for the GST system to avoid their obligations to their employees. But there are already safeguards available to employees through the general protection provisions of the *Fair Work Act 2009,*and penalties for employers who coerce employees in this way.

A similar system to this has applied in the 1990s in Queensland and the Northern Territory whereby contractors who were registered for the Federal Prescribed Payments System (a tax withholding system for contractors), were regarded as not being workers for WorkCover purposes. This definition, like GST registration, was easy to identify by the business engaging the contractors and was very clear to both parties about the implications for the entitlements to WorkCover coverage.

Businesses with a turnover of more than $75,000 are obliged to register for the GST so there would be good coverage of the industry through adopting a GST-based approach to worker determination. For contractors with a turnover of less than $75,000 who choose not to be part of the GST system, HIA would suggest that their worker status be judged by applying the Tax Office's results test.

Using the GST system in this same way would not only be of significant administrative benefit to the industry it would also remove the disputation that occurs with WorkCover, BSA, Office of State Revenue and the Portable Long Service Leave Authority around

coverage for their particular purpose. So the agencies would also benefit from a clearer and more straightforward approach to resolving a contractor's status.

For principal contractors and the regulators checking an entity's GST registration status is simple and unequivocal. The ABN look-up tool at business.gov.au provides an efficient source of GST registration data. The only other administrative test would involve establishing that the invoices charged by the sub-contractor included GST (or that the contractual arrangements provide for invoicing in this way).

Recommendation:

> *HIA would strongly urge the Committee to recommend the adoption of this GST-based approach to resolving who should be covered for workers compensation as an important first step in aligning all of the approaches to defining contractors/workers across these four government agencies.*

Employer Cannot Control Journey to Work

Workers currently enjoy workers compensation cover for their journey to and from work. The safety with which a worker operates their chosen mode of transport to and from work in most cases is something that is entirely outside the influence of their employer. It is inequitable that an employer should be meeting the cost of providing cover for these journeys and then bearing the consequences on their WorkCover ratings and premiums when a worker is injured travelling to or from work when they have no control over the workers conduct.

Recommendation:

> *Journeys to and from work should be excluded from the coverage of workers compensation or alternatively provided direct to the worker at their own expense by WorkCover. An exception would be where an employer is providing the mode of transport for a worker between different places of work, and the employer has much greater capacity to influence the conduct of the worker undertaking those journeys. In these cases it is appropriate for workers compensation to provide cover.*

Zero Premium Should Apply to Apprentices' Wages

The recent plunge in the number of apprentices in training for building trades is a major concern for the building industry and the Queensland economy more generally. There is a very real prospect that when conditions begin to improve in the home building industry that skills shortages will quickly emerge.

Employers of apprentices in New South Wales and Victoria do not pay a workers compensation premium on the wages of the apprentices that they employ. This encouragement to employ apprentices is not available to employers in Queensland. Moreover, the small businesses, who are the major employers of apprentices in the building industry in Queensland, alsodo not benefit from the payroll tax relief that is available for employers of apprentices as most of these businesses fall under the payroll tax threshold.

Exempting the wages of apprentices from and employers' workers compensation premium calculation would provide support to employers of apprentices irrespective of their size.

The savage downturn in home building activity over the last few years has placed enormous pressure on building businesses who want to maintain their commitment to training the State's future skilled workers. Exempting their apprentices from WorkCover premiums would provide a very tangible level of support.

To continue to provide an incentive for safe work practices, WorkCover premium loadings for poor performance should continue to be applied to apprentice wages: only the base wages should be exempt.

Recommendation:

> *Make apprentices' wages exempt from the calculation of employers' workers compensation premiums.*

Limitations on Public Liability Claims

Public liability insurers are increasingly becoming a back-up insurer for workers compensation claims. By way of example, it is not uncommon for an injured building worker, who is engaged by a sub-contractor on a building project, to make a workers compensation claim which WorkCover accept only then to have WorkCover pursue the principal contractor's public liability policy to offset the cost of meeting the injured worker's claim. These public liability claims will be made irrespective of whether Workplace Health and Safety Queensland have found any wrongdoing on the part of the principal contractor in the worker's injury.

The nature of the contractual chains in building projects mean that there can be many parties for WorkCover to pursue. At issue is whether there should be some limitations on WorkCover's capacity to make these claims after they have settled a claim from an injured worker.

Limiting WorkCover's ability to make public liability claims would not reduce the relief provided to injured workers as they have unlimited access to common law claims.

One possibility would be to limit WorkCover's capacity to make these public liability claims to those cases where Workplace Health and Safety Queensland have investigated the cause of an injury and fined or prosecuted a party, other than the employer of the worker, for responsibility for some part of the accident.

Recommendation

> *At the very least work should be undertaken to collect information from WorkCover and the insurers about the extent of this practice.*

Common Law Claims

Other jurisdictions apply minimum impairment thresholds for injured workers below which common law workers compensation claims cannot be made. On the grounds of simplicity and consistency having a similar provision in Queensland would be desirable. Objections to a threshold have typically relied on the impairment definition only measuring the extent to which an injured person would be unable to work, rather than assessing the impact of the injury on their lifestyle as well. A more appropriate definition of impairment could be investigated as a first step towards implementing a threshold for common law claims.

Recommendation:

> *Introduce a minimum impairment threshold for injured workers below which common law workers compensation claims cannot be made after a thorough assessment of the utility of the current impairment measure.*

Structure of Policy and Administration

HIA understands the need to separate the regulatory and monitoring functions of Q Comp from the administration of premium collection and claims management by WorkCover. However the structure of the workers compensation system does become more complex when the policy development and the workplace health and safety functions of the Department of Justice and Attorney General are overlayed. While these Departmental functions need to remain apart from the operations of WorkCover it is less clear why they need to be separate from Q Comp.

There may be some efficiency gains in monitoring the workers compensation scheme's performance and in the development of policy to have these Departmental functions merged with the responsibilities of Q Comp. Whether such a merged entity should sit within the Department or a statutory body should also be considered.

Recommendation:

> *The workers compensation policy development and workplace health and safety responsibilities of the Department of Justice and Attorney General should merge with the functions of Q Comp.*

Conclusion

In comparison with the workers compensation arrangements in other states the Queensland system performs well, especially on the financial front. However HIA believes that there is still room for some fundamental reforms around who is covered by workers compensation that would dramatically reduce the uncertainty and red tape that building industry employers currently face in administering their workers compensation responsibilities.

Attachment A

Aligning Contractor/Employee Definitions Across Queensland Government Agencies

Background

There is a high incidence of contracting arrangements in the delivery of new homes and renovations. The ever-shifting workplaces, large range of skills involved and volatility in demand all make traditional employment relationships unviable for most home building and renovation businesses. However most regulation impacting on the building industry has been designed for businesses where the traditional employment relationships dominate.

The regulatory challenges for businesses in the home building industry stem in large part from the multiple and administratively complex approaches taken to resolving who is a contractor for the purposes of a particular piece of regulation. The definition of a contractor is different for payroll tax, WorkCover, long service leave, superannuation and contractor licensing purposes. This causes confusion, high administrative costs, and under and over-reporting of obligations.

A business in the home building industry that engages a contractor needs to account for the possibility that the contractor they engage may meet all the common law tests of not being an employee but could be captured by the coverage of any or all of:

- Superannuation guarantee payments at a Federal level; and
- At a State level
    - Payroll tax
    - Workers compensation
    - Portable long service leave
    - Contractor licensing through the Building Services Authority

In organising its own affairs the contracted business also needs to examine whether it is covered by

- The workers compensation policy of its principal or whether it needs to make its own arrangements for cover; and
- The Federal alienation of personal income rules which limit its potential to make business-related tax deductions

While there may be some justification for agencies with different objectives having different approaches to contractors, for businesses engaging those contractors the outcome is costly

to administer and even more costly if mistakes are made in judgements about who is a contractor for which purpose.

Moreover, determination of a contractor's status for most regulatory purposes involves an element of judgement rather than an application of transparent rules; for example, how many materials need to be supplied in a contract for labour to not be the "substantial" part of the contract; or how "ancillary" does labour have to be to the supply of goods in a contract. This adds to the complexity of managing the regulation and increases the risk to a business where the wrong judgements might be made.

An alignment of contractor definitions across agencies would be a significant piece of red tape reform for the home building industry, and probably for many other industries as well.

Current Approaches in Queensland

The four main regulatory bodies that impact on the engagement of contractors in Queensland are

- WorkCover;
- Office of State Review (for payroll tax); and
- Q Leave - The Building and Construction Industry (Portable Long Service Leave) Authority
- Building Services Authority

All four agencies have very different approaches to resolving whether contractors should be captured within their sphere of operation.

- WorkCover relies on a hierarchy of tests involving the nature of the contract, the business structure, the extent to which it is for "substantially labour only", and the results test;
- Office of State Revenue relies on arbitrary rules about how many days in a year that a contractor works for the principal who engaged them, irrespective of the business structure;
- Q Leave relies substantially on whether the nature of the work is covered by an award in the building industry and the nature of the business structure;
- The Building Services Authority's approach is to use a range of indicia akin to a common law employment test.

The payroll tax approach to assessing contractors was "harmonised" with the New South Wales and Victorian approaches in 2008. This may have provided some benefit to the few home building businesses that operate across state borders. But for the overwhelming majority of home building businesses that only operate within Queensland it introduced an extraordinarily complex accounting exercise: home builders typically would not know how many days on site one of their contractors was engaged – they contract for a result not for a pre-determined number of days of work.

The major difficulty that the home building industry has faced with the definition of a "worker" to be covered by a WorkCover policy is that the definition has evolved in recent years as Court decisions continue to expand the scope of "worker" beyond its original intent. This has added a whole new layer of uncertainty and risk for home building businesses. It is

impossible to accurately assess how the Courts might assess a contracting arrangement in advance: whether an incident involving a contractor triggers a WorkCover claim can only be assessed at the time that an incident occurs. There is ongoing confusion about what constitutes "substantial" and even "labour" in the context of applying the substantially labour only test, for example if a contract accountant provides skill rather than labour for WorkCover purposes and so is excluded from coverage yet an electrician or plumber is regarded as only supplying labour.

The long service leave scheme covers employees and "labour-only sub-contractors" engaged in on-site building work. As with WorkCover issues arise around Q Leave's interpretation of what is "substantially labour only".

The Building Services Authority's approach that is based on common law-type checklists is different again. Unlike WorkCover and the Office of State Revenue the incentive for the BSA is to assess someone as being a contractor rather than a "worker" so that action can be taken against unlicensed contractors: the other agencies' tendency is to find contractors to be workers for the additional revenue this generates. But the existence of this fourth approach to resolving who is a contractor does add considerably to the confusion in the industry.

It is very common for a building industry contractor to be deemed not to be a contractor for one or more of these four agencies but not by the other(s): it is not just an academic difference.

All of these approaches to determining coverage of contractors in the particular regulatory regime involve a degree of judgement. There are no clear and unambiguous interpretations of how each of these schemes might impact on any one contractor. The penalties for a business engaging a contractor for making the wrong judgement about a contractor's coverage can be substantial. Under and over-reporting of obligations is also likely.

HIA also believes that the multiplicity and complexity of definitions gives rise to the occasional accusations of "sham contracting" in the industry despite the lack of any genuine evidence that the problem is real. Building unions have their own interpretation again of what constitutes genuine contracting.

The existence of all of these approaches to determining a contractor's status adds considerably to the burden that each of the regulators has in educating the industry about their unique approach. The four different definitions also add enormously to the administrative burden of businesses who engage contractors. Multiple definitions also gives rise to multiple reporting requirements by principal contractors. WorkCover, Q Leave and OSR all require annual returns of contractors who have been engaged by a principal. No two of these reporting obligations are the same.

The savings for Government and industry from a common approach to a definition of a contractor would be substantial.

A Standard Definition of Contractor

HIA accepts that no one definition of a contractor will be perfect: there is an inevitable trade-off between simplicity and precision in whatever approach is taken. But HIA is strongly of

the view that the benefits of a single definition outweigh any loss of precision, (to the extent to which the four current approaches are precise for their own purposes).

HIA believes that the industry and Government will be best served by a single indicator that

- Is well known in business;
- Can be administered simply, predictably and cheaply;
- Minimises disputes over categorisation as a contractor or not;
- Is a good proxy for all of the indicators of who is a contractor;
- Does not move any of the four agencies too far from their policy intent; and
- Can be readily communicated to principal and sub-contractors in the industry.

HIA suggests that none of the current four approaches to determining a contractor's status is ideal. Simpler options for a single definition include:

> *Common law tests* – Definitions based on common law, like the BSA's, are the most comprehensive. This approach was also used for payroll tax prior to the harmonisation changes and proved to be a good operational approach for the building industry. The Federal Workplace Relations Act also relies on common law definition of an employee for its coverage. Common law is also one of the initial filters in describing coverage for WorkCover even though the "Worker" definition is much broader than a common law employee. HIA understands that common law definitions do cause uncertainty in some other industries.
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> *Results test* – this is part of the Personal Services Income tests used by the Australian Tax Office and is also one of the tests used by WorkCover. There are three components to this test: working for a result, providing tools and equipment, and responsible for rectifying defective work. These three tests are usually built into contract documentation for contractors but are difficult to apply where the documentation is poor.
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> *GST registration* – used as one indicator of contractor status by the BSA

Of all of the indicators used by the four State agencies, the one that best meets these criteria is one of the indicators used by the BSA, namely registration for the GST system.

HIA proposes that an entity, incorporated or not, that is registered for GST with the Australian Tax Office and which charges its principal GST on its invoices should be regarded as a contractor for the purposes of all four agencies.

HIA would argue that where an entity meets these criteria they have an intention to be in business rather than be an employee. Additionally the business engaging their services expects to be able to treat the entity as contracting business.

Critics may suggest that if this approach was adopted employers would compel workers to register for the GST system to avoid their obligations to their employees. But there are already protections available to employees through the Fair Work Act and penalties for employers who coerce employees in this way.

A similar system to this has applied in the 1990s in Queensland and the Northern Territory whereby contractors who were registered for the Federal Prescribed Payments System (a

tax withholding system for contractors), were regarded as not being workers for WorkCover purposes. This definition, like GST registration, was easy to identify by the business engaging the contractors and was very clear to both parties about the implications for the entitlements to WorkCover coverage.

Using the GST system in this same way would not only be of significant administrative benefit to the industry it would also remove the disputation that occurs with WorkCover, BSA, Office of State Revenue and the Portable Long Service Leave Authority around coverage for their particular purpose. So the agencies would also benefit from a clearer and more straightforward approach to resolving a contractor's status.

For principal contractors and the regulators checking an entity's GST registration status is simple and unequivocal. The ABN look-up tool at business.gov.au provides an efficient source of GST registration data. The only other administrative test would involve establishing that the invoices charged by the sub-contractor included GST (or that the contractual arrangements provide for invoicing in this way).

Implications of this Standard Definition

Adopting this GST registration test for determining a contractor's status would reduce the number of entities that would be covered by WorkCover under the current complex and uncertain definition; but coverage would become very clear to all the parties involved. There would be a corresponding reduction in the premiums collected by WorkCover and a significant reduction in WorkCover's administrative load, audit activity and dispute management. The net impact on WorkCover's net financial position would be positive.

For Q Leave there would also be a net financial benefit as the number of people covered by the Scheme would reduce but the revenue from the levy payments would not need to change. This would assist in returning Q Leave to a financial surplus more quickly and could avoid any need for increases in the rate of levy.

There would be a reduction in payroll tax collections as fewer businesses would be captured than by the current complex definition but compliance would improve through the simplicity of the tests.

For the BSA there would be the potential for some very small scale contractors (under the $75,000 turnover limit below which GST registration is optional) to avoid being licensed, but the BSA's compliance work would be simplified. The net impact on the BSA's finances would be likely to be modest.

Action Required

Aligning the four current approaches to determining who is a contractor would require amendments to the agencies' legislation. Ideally these changes would be simultaneous.