

Engaging Freelancers, Contractors and Consultants

Don't be caught out by the Muscat judgment



The voice of freelancing

PCG: supporting and protecting freelancers, contractors and consultants

Employment status in the UK is not governed by the laws passed in Parliament: instead, it relies on common law, as developed in the courts. With judgments such as Cable and Wireless v Muscat (2006), James v London Borough of Greenwich (2008) and Dacas v Brook Street (2004), this law has become increasingly unclear recently, and the Government shows no inclination to remedy the situation.

Some companies have become hesitant about engaging freelancers and contractors for fear they might owe these workers employment rights. They have either stopped taking contractors on so readily, or started terminating their contracts after 48 weeks or 11 months in an attempt to avoid employment rights.

PCG advises that this approach is unnecessary, counter-productive and very likely to fail: by following the simple steps outlined here however, you will be able to engage freelancers and contractors with confidence.

Key points

When engaging a freelancer or contractor, always:

- use proper business-to-business terms
- ensure that their terms include the right to substitute, no "mutuality of obligation" and no direction and control – these are the key employment status tests in the common law
- ensure working practices reflect the contract and use Real Arrangements Letters to set out the practical aspects of the relationships with your contractors

Engaging Contractors: Frequently Asked Questions

What does "engaging a contractor properly" entail?

- Ensure you establish a proper business-to-business relationship with your contractors
- Make sure that their contracts

are proper contracts for services and not contracts of employment

- Make sure that the working practices of contractors on the ground are clearly distinguishable from the working practices of your staff

Is it true that a contractor can sue me for employment rights if they do work for me for more than 12 months?

- Not really: no contractor should be suing you for employment rights, although occasionally people go freelancing without realising the implications and continue to think of their clients as "employers"
- For a contractor to sue you for unfair dismissal or any other employment right, they will have to show that they were in fact your employee
- If you have a proper business to business relationship this will be impossible

Wouldn't it be better to terminate all my contractors at 48 weeks, just to be on the safe side?

- Absolutely not. If you do this with work still to be done, you will have all the extra expense of engaging new contractors and having them take time to get up to speed on work that your existing contractors could have finished more quickly and therefore more cheaply
- It is also totally unnecessary – a contractor engaged properly will never be able to claim employment rights successfully

What about the Muscat case?

- In this case, a contractor successfully sued his client for employment rights
- If you have engaged a contractor under employee-like terms Muscat may well make them your employee
- Nevertheless, proper business-to-business relationships are definitely unaffected, so to be safe, ensure you use them

So is it just a matter of what the contracts say?

- No - the contract MUST be an accurate reflection of what actually happens
- It is also a good idea to use Real Arrangements Letters, which set out the practical arrangements relating to the contract and are signed by you and the contractor – these are often considered by Employment Tribunals

What if I want to take one of my existing employees on as a contractor?

- Be very careful: ensure their pattern of behaviour is not the same as before, reflecting that they are no longer your employee, and that the contract is business-to-business
- Be aware that it will be easier for them to leave your company and go and work elsewhere if they are engaged under a commercial contract

What if an employee approaches me asking to "go limited"?

- Be very careful: if they want to do exactly the same work in the same way but via a contract, they are probably just trying to

save on tax – they will probably fall within the IR35 legislation, which would negate any tax saving anyway

- If you do agree to their request, ensure their pattern of behaviour is not the same as before, reflecting that they are no longer your employee, and that the contract is business-to-business
- If you agree to their request but their working relationship with you remains unchanged other than the introduction of a new contract, you could end up being sued for employment rights should you dismiss them
- In this scenario a court may decide that you should have been paying employer’s National Insurance Contributions and HM Revenue and Customs could approach you for this money

I have work that needs doing: what type of worker should I engage?

You have two basic choices when deciding how a new project or workstream should be carried out: a commercial supplier (freelancer or contractor) or an employee. The different considerations for each group are set out in the table below.

When you have decided which type of worker you wish to engage, set up the appropriate relationship. Remember the key employment status tests:

Personal service

- Employees will be obliged to do the work personally themselves
- Commercial providers are not under this obligation: ensure your contractors may send substitutes if necessary

Mutuality of obligation

- Employees are obliged to turn up and you are obliged to pay them

- Commercial providers are not obliged to turn up if there is no further work and you are not obliged to pay them or offer them any further work in this situation

Direction and control

- Employees may be directed in how to carry out their work
- Commercial providers should be left to exercise their professional judgment in how to carry out their work.

Remember that in a dispute courts will look at contracts to infer your intention when engaging a worker: if your intention was to hire an employee by other means – as happened in Muscat - the courts will find against you.

If in doubt, please contact PCG for advice on how to engage freelancers and contractors with confidence.

Employees	Freelancers / contractors
When to use them For ongoing and permanent work, and when you wish to control how the work is carried out.	When to use them For projects or work of a limited duration, when you need skills you don't have in-house and when you want the worker to use their professional judgment in doing the work.
Working practices It is common for employers to provide employees with all the necessary equipment and facilities they will need to carry out their duties.	Working practices Even though they may spend a lot of time on your premises while carrying out their work for you, most contractors will not wish to be integrated into your workforce to any great extent.
Obligations Employees are entitled to employment rights including sick pay, holiday pay, parental leave and protection from dismissal; some apply after certain lengths of service. You will also need to consider pension contributions, employer’s NICs and insurances.	Obligations You will not have to pay any National Insurance Contributions, holiday pay or any other employment benefits to a contractor: they will take care of all of this themselves.
Contracts Employees are engaged using a contract of service, under which the employee agrees to perform work themselves and as you instruct them.	Contracts Contractors work under contracts for services, under which they agree to provide services to your company.

About PCG

PCG was founded in 1999. PCG membership includes insurances, access to free tax and legal helplines, advice manuals, online members’ forums and standard contract templates, plus discounted legal, accounting and insurance services from PCG Affiliate members.

PCG’s extensive advice on starting out as a freelancer is available to download for free from our website.

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