

Your first worker – to employ or contract?

Wade Pearson

You can't start a business alone. Bringing your first worker on to the team is a big moment, which can make or break an early stage business. One key decision is whether to employ or contract someone. Getting this wrong can have serious consequences. In this article, we'll look at why and how to employ or contract a worker for your business.

Employee or contractor?

So what are the differences between employees and contractors? Most readers will be familiar with employment, but not everyone will have worked as an independent contractor. There are four main differences: intention, control, integration and economic reality. Imagine two examples on the opposite ends of the spectrum: a fast-food worker, and a freelance event caterer.

What do you and the worker intend?

You need a written agreement with anyone you hire. The agreement is a good indicator of intent, but it's not the whole picture. Many businesses are caught out where the agreement doesn't match reality.

How much control do you have?

A fast-food worker does what the boss says. He turns up on time, wears a uniform and cooks food to specific instructions. An event caterer has far more control over when and how she performs the services. She needs to meet her client's expectations, but will probably control the menu and might only offer services when it suits her. When you're hiring someone, carefully consider how much control you actually need to have.

How well integrated is the worker?

Think about the services the worker provides – are these fundamental to your business? Is the worker integrated into your business, or can the business operate effectively without them? Can they easily work for others?

Fast-food workers are integrated – they prepare the food a business sells. If they don't make the food, the business has nothing to sell. But an event caterer's work is probably not essential to their client's business. An event caterer will work for many different clients, not just one business. If your business would grind to a halt without the worker, then this might indicate employment.

What is the fundamental and economic reality?

The simple version of this test is: is the worker in business on their own account? Do they invoice for their services, meet their own costs (factored into their price), pay their own tax, provide their own equipment... the list goes on. None of these are determinative by themselves, but they all factor into the bigger picture.

What happens when things go wrong?

The short answer is that treating an employee as a contractor can cost you tens of thousands of dollars if the worker makes a claim against you. We've seen businesses that could have avoided messy legal battles, if they had simply obtained a few thousand dollars of advice earlier on.

The above examples are pretty simple, but what about courier drivers, or game developers, or TV technicians or film contractors? You may have seen various court cases and law changes in the news – this is an area that is constantly changing, meaning you need to be constantly on your game.

What does this mean if I'm hiring a worker?

If you're planning to hire a worker, it pays to do your research. A quick, early conversation with a lawyer might save you a lot of trouble down the road. Ultimately, when it comes to employment, good advice is worth the cost. Even if you don't engage a lawyer, there are a lot of good resources online to help you.

For an early stage startup, you may want to contract first and hire later. It's an oversimplification, but contracting generally gives you more flexibility at an early stage (if you do it right). Many businesses will hire someone as a contractor and then move to employment once it's clear that the business and the worker go well together.

This may not be appropriate for you though. You always need to apply the tests (and ideally get advice) to ensure contracting is correct in the circumstances.

Working relationships change over time too, so you should revisit the contract later on to make sure it still reflects reality.

The distinction between contractor and employee can be difficult. Luckily there is free and paid help available – investing in understanding the difference now can really be worth it later on.

Wade Pearson is a Senior Solicitor in the commercial team, at law firm Gallaway Cook Allan. This article is general in nature, so don't use it as a substitute for legal advice.