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EMPLOYEES vs INDEPENDENT CONTRACTORS

Understanding the distinction between contractors and employees and the re-characterisation of a contractor into an employee

An L&E GLOBAL Publication

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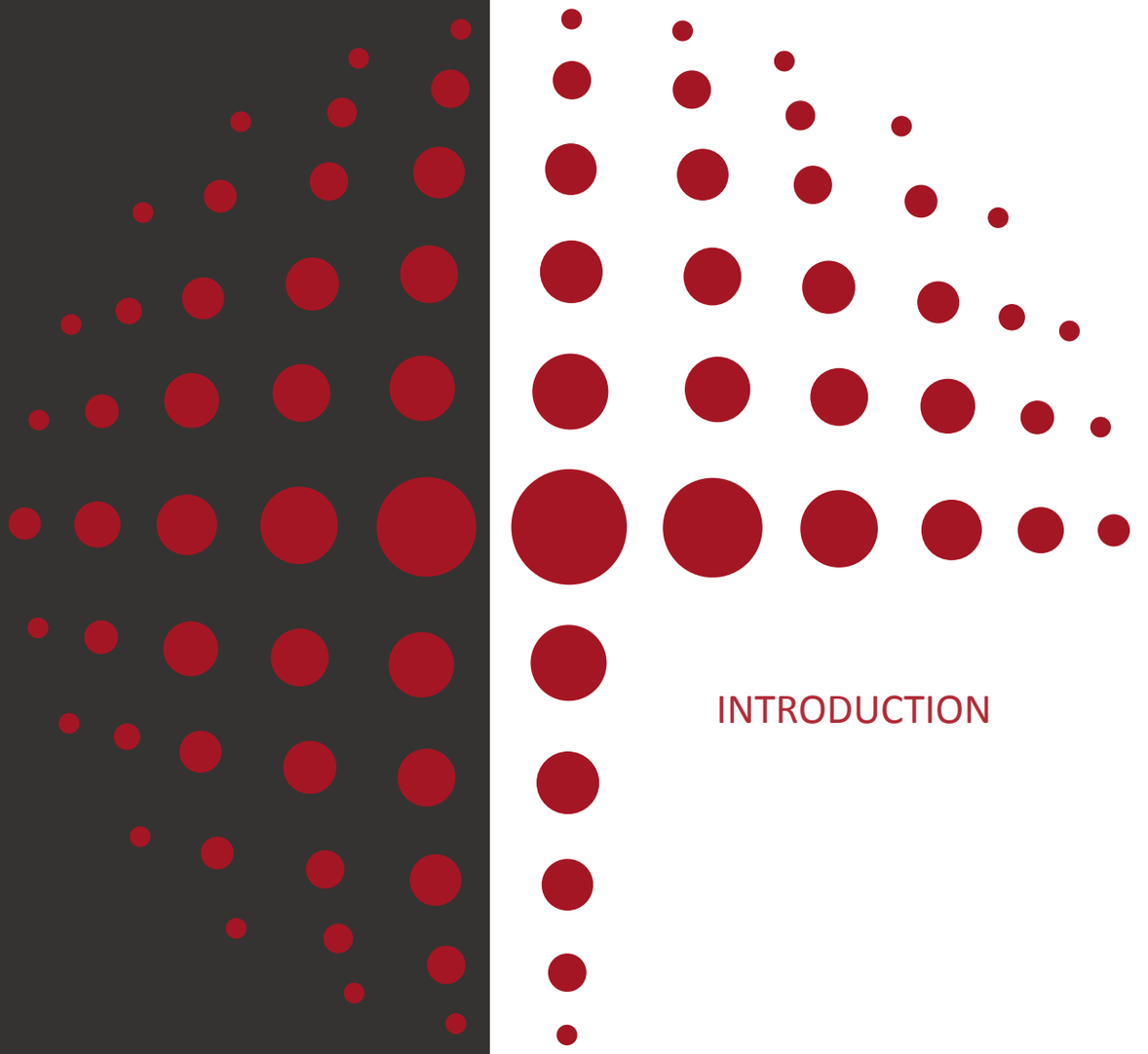

INTRODUCTION

Since we last touched upon the issue of employees vs independent contractors and the consequences of the re-characterisation of a contractor into an employee back in 2014, there has been a universal effort to eliminate sham contracts, which seek to hide the true nature of the relationship as an employer and employee agreement. Sham contracts are generally utilised so that the employer may avert the costly burdens of guaranteeing employee benefits, such as paid leave (holiday, maternity, paternity, etc.), having to pay the employer's social security contributions and income taxes on wages, and refraining from hiring unskilled, and at times undocumented migrants, who lack the bargaining power to safeguard their rights as workers.

Despite the risks of re-characterisation, in recent years, the use of independent contractors has increased significantly. So too has the use of fixed-term contracts, temporary commercial agency agreements and labour outsourcing services. This trend is not without its faults. The rise of the on-demand sharing economy (online business transactions) in areas such as carpooling, apartment/home lending, peer-to-peer lending, reselling, co-working and talent-sharing and the enterprises that drive these new workforces, including Uber, Didi, Bpost, Airbnb, Snapgoods and Zaarly, … has led to an increase in litigation, with the qualification of the contracts and work agreements as the central issue.

Surprisingly, there are several similarities between nations with regards to the definition of an "employee" and the classification of an "independent contractor". Generally, an employment contract is defined as an agreement by which an individual works for another person (natural or legal), under the latter's subordination, for which s/he receives remuneration. On the other hand, it is likely that an independent contract applies if an individual is responsible for organising his/her own workload and occupational activities, without being subject to the 'authority' of another.

Presented with an employee vs independent contractor situation, the most important distinction revolves around the concept of subordination, wherein the relationship is characterised by performance of duties under the authority of an employer who has the power to give orders, monitor execution of assigned duties and punish his subordinate's breaches of duties. To determine whether subordination exists, it matters less how the parties define their relationship in their agreement, but rather, the most important factor is the reality of the situation, i.e. whether or not subordination actually exists based on the actions of the parties.

Concluding that the circumstances warrant a re-characterisation (to change the status of a contractor into an employee or an employee into an independent contractor), certain legal consequences will apply, both for the self-employed person and the other party, with regards to tax (payments and arrears), social security (payments and arrears), and labour relations (civil or even criminal fines).

So what steps can an employer take to effectively establish an independent contractor relationship?

- a contract for service should be devoid of any kind of control or supervision from the principal employer or employer, as the case may be. Therefore, such employers should avoid involvement in day-to-day management of the work undertaken by the independent contractors and contract labourers.
- payment should be based on specified deliverables/results being achieved.
- limit the assignment. The agreement should not make inferences to, or guarantee, the length of assignment or future employment.
- the contractor should be free to contract with and do work for other companies.
- the nature of the services, the apportionment of risk, remedies in the event of breach, and liability for taxes, should be clearly and expressly provided for.

A well-drafted contract will not be sufficient to protect a company from an adverse finding of sham contracting. The substance of the relationship, as evidenced by its day-to-day nature, must also be maintained. The principal should therefore ensure that its managers manage the relationship with the independent contractor in a manner that is consistent with its independent nature, rather than in the same manner and with the same expectations that the Principal may have of its own employees.

Furthermore, it is important to prepare for the possibility that the nature or characterisation of a relationship may be questioned. To that end, it may be useful to keep a record of any information that supports a verbal contract or the interpretation of a written contract, this may include; email communications, notes from meetings, quotes from conversations, diary entries, lists of specifications and any form of reporting or tasks lists.

For employers with operations in multiple jurisdictions, successfully entering into a working relationship, whether with an employee or an independent contractor, is a very real challenge and one that impacts every sector of industry, in every region of the world. To that end, L&E Global is pleased to present our 2017 Global Handbook, which serves as an introduction to the complex issue of employees vs independent contractors, with analyses from 32 key jurisdictions, across 6 continents.

CANADA

I. Overview

a. Introduction

In Canada, companies have increasingly sought to classify workers as independent contractors in an attempt to reduce costs and administrative obligations. Workers generally do not oppose this classification as a result of favourable tax treatment enjoyed by contractors and other small businesses.

Unfortunately, most independent contractors in Canada are misclassified and many would be deemed employees if the arrangement between them and the company retaining their services was reviewed by a governmental authority or court. Often, such a review occurs when a worker has the contract arrangement terminated and seeks employment termination or employment insurance benefits.

Misclassification of workers can have profound consequences for both the company and the wrongly classified worker. Accordingly, the importance of understanding the classification of workers as employees or contractors has increased in recent years.

Classifying a worker as an employee or an independent contractor in Canada involves a complex assessment of the true nature of the working relationship. Courts and adjudicators have established a complicated and flexible analysis for making such a determination. The importance of making a correct classification cannot be understated. It is hoped that the following will assist companies and workers in making proper classification decisions and avoiding the financial liability associated with misclassification.

II. Legal Framework Differentiating Employees From Independent Contractors

a. Factors that Determine Who is an Employee and Who is an Independent Contractor

Determining whether an individual is an employee or an independent contractor under Canadian law is more of an art than a science. In simple terms, actions speak louder than words. A well-drafted and properly executed contract will not be determinative in evaluating the status of the relationship between the individual in question and the company retaining his or her services.

In making status determinations, Canadian courts and administrative tribunals will consider the subjective intention of the parties, which may include a written contract, along with the objective reality of the working relationship. The weight that Canadian courts and tribunals place on a written contract varies.

In a recent decision, the Federal Court of Appeal restated the legal test applicable to determining whether an individual is an employee or an independent contractor[1]. The current test articulated by the Federal Court of Appeal is encapsulated by the following two-step inquiry:

- first, the court should determine the subjective intention of the parties by written agreement or conduct; and
- second, the court should ascertain the objective reality by evaluating whether the facts are consistent with the parties' stated intentions.

1 1392644 Ontario Inc. (Connor Homes) v Canada (National Revenue), 2013 FCA 85 (“Connor Homes”).

In addressing the second step, decision-makers will often consider the following four factors enunciated in the case of "*Wiebe Door*", (frequently referred to as the "*Wiebe Door*" factors):

- control
- ownership of Tools
- chance of profit
- risk of loss[2]

The courts have repeatedly held that no particular factor is dominant.[3] Instead, these four factors constitute a non-exhaustive list, and there is no set formula as to their application. The relative weight of each factor will depend on the particular facts and circumstances of each case.[4] In this respect, the courts will consider all factors, and will evaluate the totality of the relationship on a case-by-case basis. In applying the Wiebe Door factors, the courts will consider some or all of the following questions for each factor:

Control
Is the worker under the direction and control of another regarding the time, place, and manner in which the work is performed? Is the worker hired, given instruction, supervised, controlled, or subject to discipline? Does the worker set his or her own hours and complete work independently? Can the worker hire subcontractors to complete the work? Arrangements whereby the worker is given greater flexibility over how and when the work is performed tend to suggest an independent contractor relationship.

Ownership of Tools
Does the worker use tools, space, supplies or equipment provided by the company or does the worker utilize his or her own resources to complete the work? Arrangements whereby the worker supplies his or her own highly specialized and/or expensive equipment may suggest a non-employment relationship. Arrangements whereby the company supplies most of the resources may suggest an employment relationship.

Chance of Profit
Can the worker increase his or her earnings by using entrepreneurial skills? Is the worker paid an hourly rate, which limits his or her chance of profit, or is he or she paid piecemeal, meaning greater efficiency may increase profits? Arrangements whereby a worker's skills, efficiency, or entrepreneurial work can increase the worker's earnings tend to suggest an independent contractor relationship.

Risk of Loss
Is the worker at risk of losing money if the cost of doing a job is more than the price charged for it? Is the worker at risk of not being paid if the work is not done correctly? Arrangements whereby workers are at a greater risk of loss when performing services may favour a finding of a non-employment relationship.

In considering the above, it is clear the courts will consider status issues on a case-by-case basis by evaluating all relevant facts and circumstances. A contract will not ensure a particular status if the practical reality is not consistent with that status. To make matters more complicated, a determination in one forum may not always be binding in another.

For instance, a finding in the Tax Court of Canada (the "Tax Court") that an individual is an independent contractor may not result in the same finding under employment standards

2 These factors were enunciated in Wiebe Door Services Ltd v The Minister of National Revenue (1986), 87 DTC 5025 (Fed CA) ("Wiebe Door") and 671122 Ontario Ltd v Sagaz Industries Canada Inc., [2001] 2 SCR 983 ("Sagaz").
3 See for instance Wiebe Door and Sagaz.
4 See Sagaz, supra at para 48. Risk of Loss

legislation. Indeed, despite the importance of correctly characterizing an employment relationship, there is no universal definition of "employee" in Canadian legislation. The Supreme Court of Canada has stated that when courts and tribunals are examining whether or not a particular individual is an "employee", the particular policy objectives of the statute at issue must be taken into account.[5]

b. General Differences in Tax Treatment

There are many tax advantages for both companies and individuals in classifying workers as independent contractors rather than employees.

For companies, payment will be made directly to the independent contractor, without any required source deductions. Also, companies will not be required to make deductions or employer contributions to various government programs, namely, for Employment Insurance ("EI") or the Canada Pension Plan ("CPP") premiums.

For the independent contractor, the lack of deductions means more money in his or her pocket. The totality of income tax and premium deductions can be significant, so the independent contractor benefits greatly from reducing and deferring the income tax payable, and from never having to make EI or CPP contributions unless he or she qualifies for, and opts into, a corresponding program.

Independent contractor status also provides the independent contractor with other tax advantages. Independent contractors can write off various business expenses, which may include home-related expenses such as internet, phone, utilities, and even a portion of mortgage/housing rental fees, along with business equipment, business use vehicles, gas, meals, and sometimes entertainment. This means that the independent contractor has the potential to net far higher earnings than an employee earning a similar gross amount.

The possibility of savings for the company does not come without risk. A company can face significant liabilities if the Canada Revenue Agency ("CRA") determines that an individual who has been treated as an independent contractor is actually an employee. Such liabilities may be of particular concern to businesses that classify a significant portion of their workers as independent contractors (for instance, as may be seen in a taxi or tow-truck company). A reassessment in those cases could compromise the future of the business. As such, companies that contract with a significant number of independent contractors should ensure that a well-drafted independent contractor agreement for each worker is in place, and that the practical reality of the working relationship is consistent with the worker's designation as an independent contractor. Otherwise, a moderate tax advantage today could become a far greater tax liability tomorrow, as the reassessment of a worker's status could mean that the company would be responsible not only for its own premiums and deductions, but also the worker's portion that it failed to remit.

In this respect, there may be advantages to classifying a working relationship as employer-employee. Deductions are made by the employer, without potential liabilities relating to income tax, EI and CPP. An employer-employee classification also provides increased protection for the worker, including the ability to apply for EI benefits should he or she become unemployed.

c. Differences in Benefit Entitlement

In general terms, independent contractor status provides workers with financial/tax

5 Pointe Claire v SEPB, [1997] 1 SCR 1015.

benefits (as described above) at the cost of all other employment-related benefits. For instance, given that independent contractors are not required to pay government premiums for EI or CPP, they likewise will not qualify for receipt of these benefits. In this respect, an independent contractor will not receive government income protection (EI) for a period where they do not have work. Also, they will not receive government pension payments by way of CPP benefits, unless they elect to contribute.

Further, independent contractors are not entitled to the basic protections of employment standards legislation. This includes the benefit of vacation pay and statutory holiday pay. Employees protected by employment standards legislation are also entitled to take various paid leaves of absence, including, but not limited to, pregnancy leave, parental leave, sick leave, and family medical leave. Independent contractors have no such entitlement.

In terms of medical benefit coverage, Canada's employment standards legislation generally does not require that companies provide medical insurance benefits for employees; however, medical benefits are often provided to employees as part of a negotiated remuneration plan. It is unlikely that an independent contractor would receive medical benefit coverage, which may include provisions for long-term disability, extended health, dental, and other insurance coverage. Notably, Canadians have universal health care coverage and are not required to pay directly for most non-elective medical procedures and assessments.

Canadian jurisdictions feature workplace safety and insurance regimes to provide benefits coverage in the event of a work-related accident. Such coverage may include loss of earnings payments, medical treatment coverage, and even retraining for a new career. Generally, while employees qualify for such coverage, independent contractors do not.

There may be special status for independent contractors in various workplace safety and insurance regimes. For instance, in Ontario, individuals can apply for optional insurance for "independent operators". Not only does this benefit the contractor (aka the operator), but it also provides significant legal protection to the company, as workers entitled to benefits under the Ontario Workplace Safety and Insurance Act for work-related injuries are generally precluded from pursuing civil actions (i.e. personal injury lawsuits) to recover damages for work-related injuries. In contrast, an independent operator without optional coverage may be free to sue the company for damages in respect of a work-related injury.

d. Differences in Protection from Termination

Both independent contractor and employment relationships can be terminated; a key distinction between them as to termination involves entitlement to notice of termination.

Independent contractors are generally not entitled to notice of termination under employment standards legislation or the common law, unless their contract contains a provision that stipulates some form of notice.

Generally, employees are entitled to notice of termination. First, applicable employment standards legislation sets minimum requirements for notice and, depending on the jurisdiction, severance pay. Second, employees may also be entitled to common law reasonable notice of termination, unless a contract of employment otherwise limits notice. Reasonable notice at common law is a remedy that the courts can provide for employees terminated without notice or insufficient notice, which is more often than not far greater than the minimum statutory requirements. An employee is entitled to at least the minimum legislative standards in respect of notice and severance, if applicable,

except in the case of significant misconduct (often termed as "just cause").

Some Canadian courts have recognized an intermediate category of contractor, between an employee and an independent contractor. This intermediate category is often referred to as a "dependent contractor" because it is economically dependent on the contracting company. A dependent contractor will generally be entitled to notice of the termination of his or her contract, however, the amount of notice to which a dependent contractor will be entitled at common law is less than the amount of notice to which a similarly-situated employee would be entitled.[6]

Notably, most of the law considering status disputes has evolved out of the Tax Court; however, other adjudicators consistently consider the Wiebe Door factors and generally apply an analogous approach.

Often such cases only come forward at the end of a relationship where a former worker, classified as an independent contractor, becomes dissatisfied with the notice of termination received when the relationship ceases. Unfortunately, even though that individual may have reaped the tax benefits of independent contractor status for years, he or she may be considered an employee or dependent contractor under the above tests, and thus, be entitled to reasonable notice of termination.

e. Local Limitations on Use of Independent Contractors

The main limitation on the use of independent contractors in Canada is the risk that they will be reclassified as employees. As discussed above, an employer could face substantial legal liability if an independent contractor is found to be an employee.

Another limitation relates to work performed under a collective agreement. Where, pursuant to a collective agreement, a union holds the bargaining rights for a particular class of workers, it may be a violation of the collective agreement for the company to hire independent contractors to complete the work ordinarily conducted by workers in the bargaining unit. A company cannot circumvent a union's bargaining rights by assigning bargaining unit work to independent contractors where the collective agreement so provides.

f. Other Ramifications of Classification

Labour Relations Ramifications
Pursuant to provincial labour legislation, such as the Ontario Labour Relations Act, where an individual is considered an "employee", that individual may be included as part of an existing bargaining unit, or may be eligible to be included in an application for certification of a union. Under the Labour Relations Act, only employees, which, by statutory definition, includes "dependent contractors", are eligible to unionize and collectively bargain. Independent contractors would therefore not be eligible to participate in the collective bargaining regime.

Insolvency Ramifications
If a company becomes insolvent, whether a worker is an independent contractor or an employee can affect the priority for amounts to be paid to the worker. Pursuant to the federal Bankruptcy and Insolvency Act, as well as various other statutes, employees take priority over other creditors up to certain amounts. By contrast, independent contractors do not have the same priority.

6 McKee v Reid's Heritage Homes Ltd., 2009 ONCA 916

g. Leased or Seconded Employees

Use of a staffing agency may provide more flexibility to meet a company's staffing needs. The use of an agency may limit various liabilities, including those arising from wrongful dismissal claims. Further, the contracting company will not be required to pay premiums for EI, CPP or other employment-related benefits in respect of agency employees. However, these costs savings may factor into the fee charged by the agency.

In the event that a company contracts with or seconds employees from an agency or another company, the company should ensure that an arms-length relationship with these employees is preserved by the practical realities of the engagement. For instance, if the company controls all aspects of the work, it may be found to be the "true employer" of the agency employees, which could result in liability for various employment-related matters.

Further, even contracting with workers from an agency may not limit liabilities in certain legal venues. For instance, the contracting company may, in some circumstances, have all or at least partial liability in respect of a workplace accident. Further, a contractor could file a human rights application against the contracting firm. As such, while using an agency does provide some protection, these protections are not boundless. Given the practical realities of working relationships, a contractual relationship may be most useful for fixed-term work projects or temporary work.

h. Regulations of the Different Categories of Contracts

Employment agreements in Canada are regulated only in the sense that a court or government body (such as the CRA) can review or analyze a relationship in the course of litigation, at the request of one of the parties, or in some cases, by undertaking an independent audit. Otherwise, parties are generally free to enter into whatever sort of relationship they wish, provided they comply with the statutory requirements that arise depending on how the relationship is classified. The relationship between the parties who enter into an agreement is generally regulated by that agreement, and will not be subject to judicial or administrative review, unless a dispute arises that results in litigation.

III. Re-Characterisation of Independent Contractors as Employees

a. Laws and Guiding Principles

It is crucial that parties clearly define whether or not they have an employer-employee or an independent contractor relationship. Nevertheless, simply labelling a worker an "employee" or an "independent contractor" is not sufficient to establish such a relationship. The intention of the parties is but one of many factors that will determine how the relationship is ultimately viewed. Rather, the total relationship between the parties will be examined.

In engaging in such review, courts and adjudicators will consider the Wiebe Door factors noted above. Courts will also review the degree of economic independence in the employment relationship (that is, whether a party is carrying on business for himself/herself or on behalf of a superior). The duration of the relationship between a worker and a company is also an important factor. If an independent contractor has been providing services to a company for many years, is providing little (or no) services to other companies, and has become dependent upon the company for income, this may indicate that the worker is a dependent contractor or an employee rather than an independent contractor.

Such tests are open to a great deal of interpretation, and the aforementioned factors are not exhaustive. However, they are important considerations that will be looked at in examining the status of an employment relationship.

b. The Legal Consequences of a Re-Characterisation

The issue of whether an individual is an employee or an independent contractor is significant because an individual's status as an employee will trigger the application of a variety of statutory rights and benefits under a number of pieces of legislation.

In Ontario, for instance, employers' specific obligations to employees may arise under the following statutes: the *Income Tax Act, the Employment Insurance Act, the Canada Pension Plan, the Employment Standards Act, the Workplace Safety and Insurance Act, the Pay Equity Act and the Labour Relations Act*.

c. Judicial Remedies Available to Persons Seeking 'Employee' Status

The remedies available to those seeking employee status depend on the forum in which the status is sought.

Pursuant to the *Employment Insurance Act*[7] and the Canada Pension Plan[8], workers may apply to the CRA for a determination of their status. A ruling will determine whether a worker is "self-employed" (i.e. an independent contractor) or an "employee", and thus, whether that worker's employment is pensionable or insurable under the *Canada Pension Plan and/or the Employment Insurance Act*. If an individual is found to be an employee by the CRA or the Tax Court, he or she may be eligible for EI or CPP benefits.

Further, an individual who has been found to be an employee may be entitled to damages for wrongful dismissal (i.e. common law notice) in the courts.

In other cases, newly reclassified employees may choose to file an employment standards claim to seek remedies under employment standards legislation, such as notice and severance pay, vacation pay, public holiday pay and/or overtime pay.

d. Legal or Administrative Penalties or Damages for the Employers in the Event of Re-Characterisation

Mischaracterization of the relationship between an employer and a worker can result in liability for the employer under a number of statutes.

Tax Implications
Employers are obligated to deduct employment income at source from all employees for tax remittance purposes. Such deductions are not required for independent contractors. Where an independent contractor is subsequently deemed to be an employee, the employer may be liable for the deductions that should have been made from the worker's income. When this occurs, the CRA generally will first turn to the individual for the outstanding amounts; however, the employer will remain liable if the individual is unable to pay, or cannot be located. The CRA can assess a penalty of 10 percent of the amount of CPP, EI, and income tax an employer fails to deduct, and can apply up to a 20 percent penalty to a second or later failure to deduct in the same calendar year, if such failure was made knowingly or by gross negligence.

7 Canada Pension Plan, RSC 1985, c C-8 at section 26.1.
8 Employment Insurance Act, SC 1996, c 23 at section 90.

Pensions and Insurance Implications
CPP payments and EI benefits are both administered by the CRA. The same factors used to determine whether an individual is an "employee" for income tax purposes are also considered in determining whether an individual is an employee or an independent contractor for the purposes of the application of both the *Employment Insurance Act* and the *Canada Pension Plan*. For both CPP and EI, employers are required to make an employer's contribution, and to deduct the employee's contribution to remit to the CRA.

With respect to CPP, employers are not expected to make contributions for independent contractors. An employer who fails to deduct required CPP contributions from an employee has to pay both the employer's share and the employee's share of any premiums owing, plus penalties and interest. Therefore, where an individual who has been operating as an independent contractor is deemed to be an employee, there are significant financial repercussions for the employer.

With respect to EI, independent contractors do not receive benefits, and no contributions are required. However, it is not unusual for independent contractors to dispute their status as independent contractors after their contract is terminated. If it is determined that they were, in fact, employees, they will be eligible for EI benefits. In such circumstances, an employer may be liable for the payment of both the employee's and the employer's contribution for a period that includes the current year, and up to the three previous years, including interest and penalties.

The current prescribed interest rate (as of September 20, 2016) for unremitted income tax, CPP, and EI contributions is 5 percent, compounded daily. Interest applies to the penalties described above as well.

Workplace Safety and Insurance Act Implications
Pursuant to provincial workers' compensation legislation, such as Ontario's *Workplace Safety* and Insurance Act (the "*WSIA*"), certain individuals are entitled to benefits if they are injured while at work. Whether or not a specific individual is covered under the *WSIA* (and is thus eligible for benefits) frequently will depend upon whether that worker is considered an "independent operator" or a "worker". Workers, defined under the WSIA to include any person who "has entered into or is employed under a contract of service", are generally entitled to benefits if they are injured at work. In contrast, so-called "independent operators", or those working under contracts for services, may not be entitled to benefits under the *WSIA*, unless they voluntarily apply to the Workplace Safety and Insurance Board (the "WSIB") for optional insurance coverage.[9]

Workers may file a complaint with the WSIB against employers who do not fulfill their obligation to pay benefit contributions. In addition, the WSIB may audit employers to ensure that premiums are being paid on behalf of all workers. The WSIB has broad powers of enforcement. If an employer fails to pay the premiums in respect of a worker, the employer may be ordered to pay the amount of premiums payable for one year, and as a penalty, may be ordered to pay that amount again.[10] Employers may also be liable to a worker for any losses suffered by that worker as a result of the employer's non-compliance. As such, if an individual is injured and it is determined that they are, in fact, an employee and not an independent operator, then there may be serious implications for the employer.

Wrongful Dismissal Claims
Generally, independent contractors cannot claim damages for wrongful dismissal; however, if a court finds that an alleged independent contractor was actually an employee or a dependent contractor, that individual may be entitled to reasonable

9 Workplace Safety and Insurance Act, SO 1997, c 16, Sched A at section 12
10 Ibid at section 88(5).

notice of termination at common law or payment in lieu thereof.

As noted above, employment status issues in wrongful dismissal claims commonly arise following the dismissal of a worker who has been functioning as an independent contractor for the duration of his or her tenure with the Company. When that independent contractor realizes, for instance, that he or she is not receiving a severance package, the independent contractor may claim that he or she was actually an employee and thus should have received reasonable notice at common law.

The length of the reasonable notice period owing to an employee will depend upon a number of factors, including the age of the employee, his or her length of service, the position he or she held when he or she was terminated, and the availability of alternate employment. As stated above, dependent contractors will generally be entitled to less notice than employees.

Vicarious Liability of Employers
In general, an employer is vicariously liable for the acts and omissions of an employee where such acts or omissions are committed by the employee "in the course of employment". By contrast, employers generally are not vicariously liable for the actions of an independent contractor. If an independent contractor is found to actually be an employee, the employer may then be liable for the acts and omissions of that individual.

IV. How to Structure an Independent Contractor Relationship

a. How to Properly Document the Relationship

Before engaging the services of a worker, an employer should first and foremost consider what relationship it wishes to establish with the worker. The employer should then draft a written agreement that reflects the Wiebe Door factors. Employers who wish to enter into an independent contractor relationship with a worker would be wise to structure the relationship in such a way as to include as many factors indicative of an independent contractor arrangement, and to exclude as many factors indicative of an employment arrangement, as possible. The terms of the relationship should be clearly set out in a written agreement that explicitly states what type of relationship the parties wish to enter into. In the case of an independent contractor, the agreement should be titled "Independent Contractor Agreement" or "Contract for Services" (as opposed to a "Contract of Service"). As previously mentioned, a written agreement between the parties will not be determinative of the relationship, but will nevertheless play a role in establishing the nature of that relationship.

The agreement should also include legally enforceable termination provisions. It may be prudent to limit the independent contractor's entitlement on termination to the minimums set out in applicable employment standards legislation, to mitigate the risk that an independent contractor may be found to be an employee.

Both the employer and the worker must act within the relationship described in their written agreement. In the event a relationship is assessed, it will not be helpful if the agreement between the parties is titled "Independent Contactor Agreement", but the parties are behaving as though the relationship is one of employer-employee. The bottom line is, if an employer wishes for an adjudicator to treat its relationship with a worker as an independent contractor relationship, the employer should give the worker as much independence as is reasonably possible, and should treat the worker almost as though he or she were a separate business entity.

V. Trends and Specific Cases

a. New or Expected Developments

The trend in Canada in recent years, much like the trend elsewhere, has moved towards an increased use of independent contractors and short-term contracts. In Canada, this has led to a corresponding increase in the frequency of litigation at the Tax Court of Canada, as a greater number of workers classified as independent contractors are seeking entitlement to benefits only enjoyed by employees.[11]Consequently, issues pertaining to employment status have taken on more significance than ever before.

In at least one Canadian jurisdiction, the effect of the increased level of independent contractors has been studied to determine the effect on employees and on workplaces. In 2015, the Ontario Ministry of Labour commenced a "Changing Workplaces Review" to determine whether the current employment and labour legislative schemes need to be amended to reflect Ontario's and Canada's changing workplaces. The Ministry appointed two Special Advisors to study Ontario workplaces, and to devise recommendations to bring the legislation in line with current practices. On July 27, 2016, the Special Advisors issued a report based on public consultations and submissions. The report made a large number of recommendations relating to a variety of employment issues for public consideration. One set of recommendations pertains to the proliferation of independent contractors and a corresponding increase in the number of misclassified workers. The report found that the number of employees who were misclassified as independent contractors was increasing and that the legislation needs to respond to this growing area of concern. The Special Advisors' recommendations to rectify the issue included: (i) an added burden on employers to prove that a person is correctly classified as an "independent contractor" when a dispute arises; (ii) an increase in the proactive education of workers so that they can determine whether they are employees themselves; and (iii) the inclusion of "dependent contractors" within the definition of "employee" under provincial employment legislation.

At this point in time, it is unclear whether the Special Advisors' recommendations will gain traction in Ontario or elsewhere in Canada, but if adopted, they could have a significant impact on Canadian workplaces. It will be important to monitor any relevant legislative developments, and to monitor other Canadian jurisdictions to see if any others follow suit. A change in one province may signal a larger scale change on the horizon, which would have significant implications for Canadian legal practitioners, companies, and workers.

b. Recent Amendments to the Law

Generally speaking, the law pertaining to the classification of workers as contractors or employees has not changed significantly in recent years. Canadian Courts have consistently demonstrated a willingness to adopt the Wiebe Door factors in assessing how workers should be classified. Canadian Courts have also demonstrated a willingness to elaborate on the Wiebe Door factors by adding other factors to consider, and by commenting further on the third classification category, namely, the dependent contractor category.

Stated Intent of the Parties

Canadian courts have taken varying approaches with respect to the weight that should be given to written contracts in making status determinations. For instance, some decisions heavily favour a finding consistent with the written contract agreed to by the parties, while other decisions completely ignore the same.

11 See Big Bird Truck Inc. v. Minister of National Revenue, 2015 TCC 340

Royal Winnipeg Ballet v MNR (2006 FCA 87) ("Winnipeg Ballet") suggests that substantial weight should be given to the stated intention of the parties. In Winnipeg Ballet, the Federal Court of Appeal overturned a previous decision by the Tax Court, which had found that three dancers were employees and not independent contractors.

The evidence clearly indicated that both parties understood the dancers to be independent contractors, and that the parties acted in a manner consistent with this understanding. The dancers charged a Goods and Service Tax (GST) for their services, and the employer did not withhold taxes. The agreement contained no express provision regarding the dancers' status. It set out, *inter alia*, minimum rates of pay, contributions to health care, and disability insurance. Dancers were required to pay for certain costs independently, including costs relating to rehearsal outfits and makeup, while the employer was required to pay for other costs, such as the purchase of costumes.

The majority of the Federal Court of Appeal held that "in determining the legal nature of a contract, it is a search for the common intention of the parties that is the object of the exercise".[12] The Federal Court of Appeal found that the Tax Court erred in failing to consider the parties' intention, and should have considered the Wiebe Door factors in light of the evidence that both parties had understood and acted as though the dancers were independent contractors. The Federal Court of Appeal acknowledged that the understanding of the parties with respect to status is not necessarily determinative, and noted that if the parties' stated intention is not reflected in the terms of the applicable contract and the practical reality of the day-to-day relationship in dispute, then the parties' intention will be disregarded.

The *Winnipeg Ballet* decision has been applied with varying results in subsequent decisions. In considering this varying jurisprudence, the Federal Court of Appeal in *Connor Homes* (discussed above) recently clarified the test to be applied in determining the status of a worker, as outlined above. Specifically, at paragraphs 39 to 41 of *Connor Homes*, the Court endorsed the following two-step inquiry:

> Under the first step, the subjective intent of each party to the relationship must be ascertained. This can be determined either by the written contractual relationship the parties have entered into or by the actual behaviour of each party, such as invoices for services rendered, registration for GST purposes and income tax filings as an independent contractor.
>
> The second step is to ascertain whether an objective reality sustains the subjective intent of the parties. As noted by Sharlow J.A. in *TBT Personnel Services Inc. v. Canada*, 2011 FCA 256, 422 N.R. 366 at para. 9, "it is also necessary to consider the Wiebe Door factors to determine whether the facts are consistent with the parties' expressed intention." In other words, the subjective intent of the parties cannot trump the reality of the relationship as ascertained through objective facts. In this second step, the parties' intent as well as the terms of the contract may also be taken into account since they color the relationship. As noted in Royal Winnipeg Ballet at para. 64, the relevant factors must be considered "in the light of" the parties' intent. However, that being stated, the second step is an analysis of the pertinent facts for the purpose of determining whether the test set out in Wiebe Door and Sagaz has been in fact met, i.e whether the legal effect of the relationship the parties have established is one of independent contractor or of employer-employee.
>
> The central question at issue remains whether the person who has been engaged to perform the services is, in actual fact, performing them as a person in business

12 Royal Winnipeg Ballet v MNR, 2006 FCA 87 at para. 59.

on his own account.[13]

Recent jurisprudence appears to adopt the reasoning set out in *Winnipeg Ballet and Connor Homes* and appears to support the proposition that the intention of the parties is a factor to be considered[14]. That said, it remains to be seen what weight adjudicators will ascribe to this factor relative to others in the future.

Dependence on the Employer
The Ontario Court of Appeal considered the differences between employees, dependent contractors and independent contractors in *McKee v Reid's Heritage Homes Ltd*, 2009 ONCA 916. The plaintiff in that case carried on business through her company and even engaged her own employees. Her contract, although no longer binding, seemed to demonstrate an intention that she be considered a contractor. The plaintiff was paid by commission; however, she was economically dependent on the defendant company, as she had worked exclusively for the defendant for a number of years.

The Ontario Court of Appeal considered a number of factors, including the following:

- whether the person works exclusively for the employer;
- whether the person is subject to the control of the employer;
- whether the person owns the tools of the trade;
- whether the person has undertaken risk or loss/chance of profits, as distinct from fixed compensation; and
- whose business is it?

The Court concluded that the plaintiff was an employee rather than an independent contractor or a dependent contractor. Accordingly, the plaintiff was entitled to reasonable notice of the termination of her contract.

This case demonstrates that if the worker is in an economically vulnerable position vis-a-vis an employer, there is a risk that a court will find that an employment relationship or a dependent contractor relationship exists. This decision is also notable because it sheds greater light on the intermediate "dependent contractor" category. A dependent contractor is dependent on the employer for most or all of his or her business. Dependent contractors are entitled to notice of termination, although not to the same extent as employees.

As the concept of the dependent contractor catego ry has only relatively recently been adopted by Canadian courts, it will be interesting to see how the jurisprudence in this area continues to evolve, and how courts will endeavor to strike a balance between employees and independent contractors in the future.

Status Quo in the Legislation
It should be emphasized that the case law pertaining to employee classification is largely settled, and has not undergone significant change in recent years. The same can also be said of the applicable statutory regime. The statutes discussed above, including the *Employment Insurance Act, the Canada Pension Plan, and the Income Tax Act*, have not been significantly amended as they relate to independent contractors. The legislation's application to independent contractors is minimal, especially compared to the degree to which provision is made for employees. It appears that Canadian legislators are satisfied with the status quo, and that they are satisfied with the minimal application to independent contractors.

As discussed above, it may be interesting to monitor legislative developments at both

13 Supra note 1 at paras 39-41.
14 See Porotti v. Minister of National Revenue, 2016 FCA 29.

the federal and the provincial level to determine whether dependent contractors are brought within the scope of the applicable statutes. It may be reasonable to speculate that dependent contractors will eventually be brought within the application of a broad range of employment-related legislation, such that they will be entitled to the same or similar benefits as employees.

VI. Business Presence Issues

a. How the Use of One or More Independent Contractors Creates a Permanent Establishment in Country and the Ramifications

Generally speaking, a non-resident corporation that carries on business in Canada will be subject to Canadian tax filing requirements and will be required to pay taxes on business profits attributable to that establishment.[15] However, it is worth noting that Canada is a party to the Convention between Canada and the United States of America with Respect to Taxes on Income and on Capital (the "Convention"), which may alter the foregoing default arrangement. Article VII of the Convention provides that business profits will only be taxable in Canada if the non-resident carries on business through a "permanent establishment". Article V establishes two types of permanent establishments: a "fixed place of business" or a "dependent agent". A dependent agent must have the authority, and must habitually exercise that authority, to conclude contracts in the name of the U.S. corporation. Paragraph 7 of Article V stipulates that a permanent establishment will not be created where business is carried out in Canada through a broker, general commission agent, or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

The following key factors in the dependent agent permanent establishment analysis are set out in *American Income Life Insurance Co. v Canada, 2008 TCC 206 ("American Income")*:

- did the agent have the authority to conclude contracts in Canada?
- was the agent of independant status, both legally and economically?
- was the agent acting in the ordinary course of his or her business?

With respect to permanent establishment, the CRA's views are generally consistent with those of the Organization for Economic Co-operation and Development ("OECD") in its Model Tax Convention on Income and on Capital and its Commentary. The OECD has clarified that a dependent agent must habitually exercise its authority to conclude contracts, and that those contracts must relate to the operations that constitute the "business proper" of the non-resident.

In light of the foregoing, a truly economically independent contractor in business for him or herself is unlikely to create a permanent establishment for the purposes of Canada's *Income Tax Act*. The independent contractor versus employee tests outlined above will be relevant in determining whether an agent was performing services as a person in business on his or her own account. If the agent was not in business for him or herself, then that agent must have significant contracting authority in order to create a permanent establishment.

b. How the Employment of One or More Individuals Creates a Permanent Establishment in Country and the Ramifications

The employment of one or more individuals in Canada may create a permanent establishment where there is either a fixed place of business, or where business is

15 Income Tax Act, RSC 1985, c 1 (5th Supp), at section 2(3)(b).

conducted via a dependent agent. The ramifications of the creation of a permanent establishment include that the non-resident corporation will be required to pay taxes in Canada on its business profits attributable to the permanent establishment.

An employee in Canada may create a permanent establishment where that employee has significant power to bind the non-resident corporation in contract. Such authority must extend to concluding contracts relating to the operations that constitute the "business proper" of the non-resident, and this authority must be exercised habitually. Whether an employee's contractual authority will be sufficient to create a permanent establishment will depend upon the particular facts and circumstances of each case.

VII. Conclusion

The foregoing summarizes some of the distinctions between employees and independent contractors in Canadian law.

In Canada, the line between who is an employee and who is an independent contractor is often blurred, which may have significant implications for employers. If an independent contractor is found to be an employee, the employer faces significant liability under a number of statutes, as well as under the common law. Consequently, it is imperative that the relationships between workers and the companies retaining their services be both correctly characterized under clear and legally enforceable written agreements, and correspond to practical realities that are consistent with those agreements.

Generally, the factors applied by Canadian adjudicators in assessing the status of a worker will examine the totality and true nature of the relationship in dispute. In simple terms, if an individual looks like an employee and acts like an employee, adjudicators in Canada are likely to find that he or she is in fact an employee.

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