



HELPING YOU TAKE YOUR BUSINESS TO THE NEXT LEVEL



DISCUSSION PAPER #8

**EMPLOYEE OR SELF EMPLOYED CONTRACTOR?**

**ADDING CLARITY AND VISION**

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Many companies believe that using contract “employees” provides a lower personnel cost than the traditional employer-employee relationship. The truth is that, in many cases it can cost significantly more and, even if the costs are indeed lower, use of a contract “employee” can be harmful to your business.

### **The “Benefits”**

The main reason for using contract “employees” is the belief that this will enable the business to avoid the costs and obligations imposed by the government on employers. These include:

- CPP and EI premiums
- Vacation pay
- Notice of termination
- Statutory holiday pay
- Health insurance and similar benefits
- Pension obligations
- WSIB premiums

Unless these issues are properly addressed at the outset the employer could be liable for these costs. **Even worse, they could find themselves liable for significant penalties and interest, litigation costs and liability judgements.**

### **The Rules**

The Supreme Court has determined that there are four tests that determine whether an individual is an independent contractor or an employee. Canada Revenue Agency (CRA) uses these criteria to determine if a business relationship exists between the payer and the person providing the services. These are:

1. Control: A contractor relationship implies that the control of the work is under the control of the contractor and is directed towards the attainment of a specific objective. The greater the degree of control of the work exercised by the employer, the more likely the relationship is one of employer-employee. The freedom of the “contractor” to accept other work is also an important factor in determining control.
2. Ownership of Tools: Generally an independent contractor owns his/her tools. However there are many exceptions.

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3. Chance of Profit (Risk of Loss): The earnings of an independent contractor tend to vary with the amount of work they complete. Those of an employee generally do not. If the contractor has an investment in his/her business over and above the value of the labour invested in the activity, this will usually indicate an independent contractor status.
4. Integration: If the contractor integrates the payer's business activities into his commercial activities, then a business relationship probably exists. The contractor is acting on his/her own behalf and is not solely dependent on the payer.

In order to qualify as an independent contractor, the individual must qualify on each of the four tests. If this is not the case, then either the payer or the contractor may obtain a ruling from CRA.

For those wishing additional information, please visit the CRA website at:

[www.cra-adrc.gc.ca/E/pub/tg/rc4110/README.html](http://www.cra-adrc.gc.ca/E/pub/tg/rc4110/README.html)

### **The Risks of Using Contract "Employees"**

Even if a contract "employee" meets the CRA tests there a number of issues that need to be carefully considered by your business. A potential contract "employee" who meets the CRA tests is concerned, by definition, with their own business interest over that of your company.

Inherent in the employer-employee relationship are a number of mutual duties and responsibilities. Too often the focus is on the duties of the employer, so this article will address some of the duties of the employee. In the absence of a written contract, the Common Law provides, among others for the following duties of an employee:

1. To do what a reasonable employee would do in any situation.
2. The duty of honesty.
3. The duty to obey the employer's lawful instructions.
4. The obligation not to disclose the employer's confidential information.
5. To work at all times with reasonable care and skill.
6. To look after the employer's property if using it.

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7. To not to compete in business against the employer while still in their employ.
8. To give any inventions made during their employment to the employer.

Some of these duties may even survive the employee's term of employment. While most of the above duties are generally assumed some, such as the duty not to disclose confidential information, are of great value to employers.

In the absence of a written contract, not all of these duties may apply to a contractor, especially after the end of the contract.

### **The Emotional Issue**

One of the most valuable assets a company can have is "company spirit". This spirit includes such things as loyalty to the company and fellow employees, teamwork, a willingness to pitch in when needed and a willingness to provide a high level of customer service.

Company spirit takes a long time to develop and can be easily be lost. One of the most common ways to diminish that spirit is through the use of contract "employees".

In today's environment the use of contract "employees" can be perceived by other employees as a threat to their jobs. Their loyalty is to their fellows, not to the outsider. In addition, it is common for contract "employees" not to show the same level of commitment to the company as other classes of employee. This is to be expected, as a company is showing a higher degree of loyalty to the person when it hires them as an employee than when it engages them as a contractor.

The use of a contractor may also result in lower efficiency. While a contract "employee" may not be burdened by the "this is the way we do things here" syndrome, they also do not possess the wealth of information about the company, its customers, its procedures and its culture that accumulates over time through the employer-employee relationship.

### **When does it make sense to use a contract "employee"?**

The use of contract "employees" may be advisable under certain limited circumstances. The most common situations are:

- For projects with a fixed time span and where the demand for the skills will disappear once the projects are completed. This is quite common when using engineers on large projects such as oil refineries, dams and other large construction projects.

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- To provide skills for which there is a short-term need and which are not available within the company. This is common in the information technology industry.
- To perform work that employees find unattractive, such as cleaning and janitorial.

### **Summary**

Contract “employees” may not be less expensive over the long run than regular employees and may have higher degrees of risk associated with them.

The use of contract “employees” is not conducive to the development and maintenance of “company spirit”.

Contract “employees” are preferable in certain specific circumstances.

### **We can help**

If you have questions or need assistance with this or other Human Resource issues, please contact

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