Employee or Independent Contractor

Some Recent Decisions

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Introduction

There has been a tremendous growth in the number of self-employed workers. According to one Statistics Canada study, self-employment accounted for more than three out of four new jobs that the Canadian economy created between 1990 and 1999. [1] While some of this growth may have been attributable to worker interest in flexibility, independence and tax advantages, many employers have been interested in the flexibility and cost savings offered by these relationships. The question for today is – are these people really "independent contractors?" The follow up questions is – "does it matter?"

The Traditional Distinction – Who is an Independent Contractor?

Volumes have been written about the distinction between employees and independent contractors. For common law purposes, the distinction was relevant to issues such as vicarious liability and notice of dismissal. The distinction has also been used for a range of statutory purposes – employment standards codes, labour relations codes, workers compensation legislation, and, of course, the *Income Tax Act.* Consistent with the wide number of legal purposes, courts and other decision making bodies have adopted a range of tests to determine whether a person was an employee or an independent contractor.

Employment lawyers are all too familiar with the history of the various tests that have been applied. Through to the late 1970s, the "control test" governed. This involved an examination of how much control the work provider had over the activities and conduct of the worker. Then

came the "organization test" set out by Lord Denning in *Stevenson Jordan and Harrison Ltd. v. MacDonald & Evans,* in which the key focus was whether or not the person's work was performed "as an integral part of the business," or "only accessory to it." [2] The Privy Council in *Montreal (City) v. Montreal Locomotive Works Ltd.*, [3] enunciated the economic reality or "entrepreneur test," also known as the "fourfold test." This test involved a consideration of the factors of (1) control, (2) ownership of tools, (3) chance of profit and (4) risk of loss in order to determine whether a person was an employee or an independent contractor.

In 1987, the Federal Court of Appeal, in *Wiebe Door Services Ltd. v. M.N.R.,* [4] considered an appeal from the finding of the Tax Court of Canada upholding the Minister of National Revenue's assessment for Unemployment Insurance premiums and Canada Pension Plan contributions. The court reviewed the various tests and concluded that the Lord Wright's test in *Montreal (City) v. Montreal Locomotive Works Ltd.* was not a fourfold test but rather a four in one test. The court adopted the practical approach "that in a large number of cases, the court can only perform a balancing operation, weighing up the factors which point in one direction and balancing them against those pointing in the opposite direction." [5] *Wiebe Door* has been frequently cited as the definitive authority on the employee/independent contractor issue in cases involving employer liability to the Minister of National Revenue for Income Tax deductions, Unemployment Insurance premiums and Canada Pension Plan contributions.

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[1] Zhengxi Lin et al, "The Entry and Exit Dynamics of Self-Employment in Canada," No. 134, March 1999.
[2] [1952] 1 TLR 101, at 111 (C.A.)
[3] [1947] 1 D.L.R. 161 (P.C.)
[4] [1986] 2 C.T.C. 200 (F.C.A.)
[5] [1986] 2 C.T.C. 200 at 206 (F.C.A.)

Leaving aside the Minister of National Revenue, the law has been evolving in a way that sometimes makes the traditional distinction of employee and independent contractor irrelevant – at least for some purposes.

Independent Contractors, Employees and Common Law Notice – Some Recent Cases

In the 1999 decision of ***Marbry Ltd. v. Avrecan International Inc.***, [6] Mr. Justice Braidwood, writing for the majority of the British Columbia Court of Appeal, had these insightful comments about the distinction between an employee and an independent contractor, for the purpose of reasonable notice of termination:

> "At the heart of the court's inquiry is the true nature of the relationship between the parties. All relationships in the workplace setting can perhaps be thought of as existing on a continuum. At one end of the continuum lies the employer/employee relationship where reasonable notice is required to terminate. At the other extremity are independent contracting or strict agency relationships where notice is not required. The difficulty obviously lies in determining where upon that continuum one is located. Does the relationship bear more resemblance to the employer/employee or the independent contractor status?"

Here, the court was examining the termination of an exclusive distributorship. The plaintiff corporation had been the exclusive seller of Reebok footwear and clothing in parts of British Columbia pursuant to a distributor agreement with the defendant. The plaintiff maintained its own showroom as well as a sales person. The plaintiff also performed collections for the defendant and conducted product knowledge seminars. The sale of the defendant's products represented between 75% and 90% of the plaintiff's total commissions. The defendant terminated the distributorship agreement on one month's notice. The plaintiff's action was for damages for failure to provide reasonable notice of the termination of the agreement.

The court noted that the fact that the plaintiff/employee is a corporation is not a bar to recovery. The court also adopted the principle in the Ontario Court of Appeal's decision in *Carter v. Bell & Sons (Canada) Ltd.*, which held that "there are many cases of an intermediate nature where the relationship of master and servant does not exist but where an agreement to terminate the arrangement upon reasonable notice may be implied." [7] The court noted that, in *Carter*, emphasis was placed on factors indicating a more permanent relationship in finding that the relationship was more akin to one of employer/employee than that of independent contractor. The court concluded that the relationship between *Marbry* and *Avrecan* was more akin to employee/employer than independent contractor and therefore rested in that intermediate category requiring termination upon reasonable notice. In coming to this conclusion, the court highlighted the following factors:

(i) the parties were in a relationship of permanency, lasting for 10 years;

(ii) the plaintiff invested resources in the business that indicated reliance;

(iii) at least 75% of the plaintiff's sales were earned from this relationship; and

(iv) the plaintiff's business formed "an integral part of" the defendant's business.

The Court of appeal, however, reduced the period of reasonable notice from the 15 months found by the trial judge to nine months.

Marbry Ltd. v. Avrecan International Inc. has been cited favourably in Ontario. In ***Job v. Re/Max Metro-City Realty Ltd.,*** [8] a Re/Max real estate agent claimed damages for the termination of his employment without reasonable notice. Re/Max contended that Job was an

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[6] (1999), 44 C.C.E.L. (2d) 76
[7] [1936] 2 D.L.R. 438 (Ont. C.A.) at 440

independent contractor and the relationship could be terminated without notice. The court found that the Re/Max real estate agent was not an employee based upon a consideration of the factors of control, ownership of tools, chance of profit and risk of loss and the "organization test". However, the court cited both the *Marbry Ltd. v. Avrecan International Inc.* and *Carter v. Bell & Sons (Canada) Ltd.,* decisions in concluding that the relationship was one of a permanent character and therefore subject to an implied term that it could only be terminated upon reasonable notice.

In the Ontario decision of ***Regal Produce Brokerage (1990) Ltd. v. Fowler Packing Co.,*** [9] the court considered the claim of a plaintiff corporation to reasonable notice of the termination of its relationship as the defendant's food broker. Justice Paisley quoted extensively from *Marbry Ltd. v. Avrecan International Inc.* Based upon a longstanding relationship since the early 1980's, the personal relationship between the principals of the plaintiff and defendant and the fact that the plaintiff's sole source of income from brokering was from the defendant, the court found that the relationship was of an intermediate nature where reasonable notice of termination was required.

In ***Brown v. Western Legal Publication,*** [10] the plaintiff was a digest writer who had been digesting legal cases for the defendant for twenty years. He was paid a flat amount per year, without deductions and he held himself out for income tax purposes as an independent contractor. When the defendant indicated that his remuneration would be changed to piece work, which the plaintiff calculated would reduce his remuneration by almost one-third, the plaintiff accepted the repudiation of contract and commenced an action for damages. The Court rejected

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[8] [1999] O.J. No. 5029 (Ont. S.C.J. – Panet J.)
[9] [2000] O.J. No. 676 (Ont. S.C.J. – Paisley J.)

the defendant's position that the plaintiff was an independent contractor and found, on the basis of the traditional analysis that the plaintiff was an employee. The plaintiff had worked exclusively for the defendant, and was subject to the control of the defendant for everything except hours of work and the place where the work was done. The plaintiff used the defendant's tools and supplies. Further, he took no risk and had no ownership share. Of interest is the fact that the Court noted expressly that "the fact that the plaintiff holds himself out as an independent contractor is not determinative of his status. The question here is whether or not the plaintiff is an employee for wrongful dismissal purposes…not for income tax purposes." Accordingly, the plaintiff was entitled to sixteen months' compensation in lieu of reasonable notice of dismissal.

In ***Truong v. British Columbia,*** [11] the British Columbia Court of Appeal considered the case of a court interpreter who was retained over a three year period. The plaintiff was subject to a "Court Interpreters Code of Professional Conduct," which regulated various aspects of the manner in which she would perform her work. She was called in as needed, selected on a rotational basis and paid on the basis of a non-negotiable hourly basis. No deductions were made for income tax, Unemployment Insurance or Canada Pension Plan benefits and no T4 was provided to her. She deducted expenses from her income for income tax purposes as an independent contractor. After reviewing a number of the classic decisions, including *Montreal Locomotive* and *Wiebe Door*, Hinds J.A., writing for a majority of the Court, upheld the trial decision that the plaintiff was an employee. The court approved of the statement reached in *Brown v. Western Legal Publication* that holding oneself out as an independent contractor is not determinative of status.

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[10] (1998), 51 B.C.L.R. (3d) 345 (B.C.S.C.)
[11] (1997), 32 C.C.E.L. (2d) 291 (B.C.S.C.)

Does The Distinction Still Matter – For Notice Periods?

Even if the notice-seeking plaintiff can establish that the relationship is akin to an employee rather than an independent contractor, the appropriate characterization of the relationship may still have an important role to play. One issue is whether a written contract, that provides for less notice than employment standards minimums, will be upheld. Another issue is whether the plaintiff will be entitled to less notice if the relationship is characterized as akin to an employee, but not that of an employee.

In *Machtinger v. HOJ Industries Ltd.,* [12] the Supreme Court of Canada held that the common law presumption of termination of employment on reasonable notice would be rebutted if the contract of employment contained a notice provision. This was subject to the qualification that a termination provision in an employment contract that provided less notice than the notice of termination of employment required by the applicable employment standards legislation, would be unenforceable.

However, if the relationship is an "intermediate" relationship, or some other form of non-employment relationship that would still attract notice for the termination of the relationship, does *Machtinger v. HOJ* still apply? It has been accepted in two recent Ontario cases, *Leerdam v. Stirling Douglas Group Inc.* [13] and *Hamilton v. Open Window Bakery Ltd.,* [14] that clear and unambiguous provisions in a written contract will displace the common law requirement of reasonable notice that would otherwise apply to an "intermediate" relationship.

[12] [1992] 1 S.C.R. 986
[13] [1999] O.J. No. 914 (Ont. Gen. Div. – Macdonald J.)

The issue of whether the notice provision would be unenforceable if it did not provide the notice of termination required by employment standards legislation was raised but, in my view, not answered in *Leerdam v. Stirling Douglas Group Inc*. The plaintiff was retained as an associate under the terms of a contract that contained an acknowledgement that he was not an employee. The contract provided that his services could be terminated upon one week's written notice. The contract was for a one year term with provisions for renewal. After seven months, the defendant terminated the contract with one week's payment in lieu of notice. The plaintiff claimed that he was an employee, that the notice provision did not apply and that he was entitled to damages for the balance of the one year term. Macdonald J. indicated that it was not necessary for him to decide whether the plaintiff was an employee or not as his legal position was the same in either case. He reviewed the principle set out in *Machtinger v. HOJ Industries Ltd.* and concluded that the contract was binding and that the termination provision in the contract should be enforced. Macdonald J. was of the view that given the length of employment of seven months, the Employment Standards Act [15] did not affect the contractual notice period.

If, however, the plaintiff had been retained for longer than one year, Macdonald J. would have had to determine whether the plaintiff was an employee and, if he found the relationship to be akin to an employee rather than an independent contractor, whether the notice provision was unenforceable due a failure to provide the notice of termination required by employment standards legislation.

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[14] [2000] O.J. No. 5004
[15] R.S.O. 1990, c. E.14

Since it is often difficult to accurately predict whether a relationship will be characterized as one of independent contractor or a relationship of an intermediate nature requiring reasonable notice of termination, prudence would indicate that contracts with appropriate notice provisions be used to limit liability for common law notice requirements. In drafting these notice provisions, the question to be answered is what are the minimum notice provisions that will be enforceable. To preclude an unenforceability argument, the most conservative advice would be to ensure that any notice period specified meets the minimum standard of applicable employment standards legislation that would have applied if the relationship was one of employee/employer.

There have been recent decisions concerning the notice that should be provided to an independent contractor who is in a relationship akin to an employment relationship – but is not an employee. In *Marbry Ltd. v. Avrecan International Inc.,* the court considered the factors of the length and type of relationship between the parties, the extent of the sales force employed by the party whose distributorship was terminated, the importance of the distributorship to the party terminated, the acquisition of inventory and the time needed by the terminated party to acquire a replacement line. The factors of a 10 year relationship, a sales force of one and sometimes two, a relationship accounting for 90% of its business, a small saleable inventory and an inability to find replacement products, resulted in nine months notice.

In *Job v. Re/Max Metro-City Realty Ltd.,* the court based its determination of notice on the factors cited in *Marbry Ltd. v. Avrecan International Inc.* The plaintiff, a Re/Max agent, was awarded six months notice based upon a six year relationship, the exclusivity of the relationship,

the inventory of advertising and brochures that had been acquired and the time needed to re-establish the plaintiff with another broker.

The results in the above cases do not appear much different from the results that might be obtained from the application of the traditional *Bardal* factors to a termination of employment situation. However other cases have shown a marked difference. In New Brunswick, courts seem to be of the view that, one gets one half as much notice as if he or she had been an employee. In *Erb v. Expert Delivery*, [16] the plaintiff, a four year driver, was awarded one month's notice of termination. The court noted expressly that he would have been entitled to two months notice had he been an employee. Similarly, in *Jackson v. Norman W. Francis Ltd.*, [17] an accountant who had been employed for eighteen years was awarded damages based upon nine months notice instead of eighteen months notice, because he was found to be an independent contractor.

[16] [1995] N.B.J. No. 381 (N.B.Q.B.)
[17] [1999] N.B.J. No. 147 (N.B.Q.B.)