

Contractor vs Employee

Whether or not a worker is an employee or an independent contractor may not always be apparent. Yet the distinction is an important one: employees are afforded many protections and entitlements not available to contractors. Employees can obtain damages and other remedies for unjustified dismissal, discrimination or disadvantage. They are also protected from exploitation by a raft of statutes granting them minimum entitlements in vital areas such as wages and salaries, holidays, sick and bereavement leave, and parental leave.

The entities that employ workers have numerous obligations, both in employment law and elsewhere, not least of them being to pay tax on their employees' behalf and to pay KiwiSaver contributions. It can therefore be seen that both the employment institutions and Inland Revenue have an interest in distinguishing between employers, who work under a "contract of service", and independent contractors, who work under "contracts for services", in order to ascertain the obligations of the person engaging them. It has been the practice of Inland Revenue to defer to the decision making of the employment institutions, which have in turn relied on common law tests developed over many years. As a starting point, however, the Employment Relations Act 2000 provides that the decision as to whether a person is employed under a contract of service is to be made by determining "the real nature of the relationship between them". The Employment Court or the Employment Relations Authority must consider all relevant matters including evidence as to the intention of the parties, though what the parties actually call themselves is not to be treated as a determining matter.

The difference between an employee and a contractor

There is plenty of advice online to help with differentiating between the two. Type "contractor" into the search fields of the [Employment NZ website](#) or [Inland Revenue website](#). Both have useful comparison tables.

How is being an independent contractor different from being an employee?

Independent contractors

Independent contractors are self-employed, so they:

- are not covered by the ERA or the Holidays Act 2003 (so no paid leave, minimum hourly rate etc)
- are generally contracted to work only for a specific period of time
- are responsible for their own ACC payments
- may be responsible for paying their own income tax
- may need to be registered for GST
- supply their own work-related tools and equipment
- have the right to decide how they will do the work.

The contractor's relationship with the person or organisation they do work for (their client), is covered by their contract (often called a "contract for services"). The contract for services covers how either party (the contractor or their client) can end their working relationship.

If you are thinking of working as an independent contractor, it is essential to have a written contract that covers your conditions of work.

More information

More information about the difference between contractor and employee is on the [Employment New Zealand website](#).

There is a [visual guide to staff types](#) on the business.govt.nz website which illustrates the differences between types of staff, and this guide to [going contracting](#).

You can read our information about what it means [to be an independent contractor](#).

Determining the Relationship

Through case law, a number of tests have been developed to help determine the real nature of the relationship. The starting point is what is stated in the documentation or the agreement between the parties. The following will also need to be considered:

✓ Intention of the Parties

The intention of the parties at the time of entering into the agreement. What was the intention at the time and the reasons. How has it played out subsequently?

✓ The Control Test

This looks at the degree of control the boss has over the worker. The more control the boss has, the more this tends to indicate that the relationship is employment. The less control the boss has, the more this tends to indicate the relationship is that of an independent contractor

✓ The Integration Test

This test looks at how integrated the worker is in the business. Highly integrated tends to suggest employment and low integration is more likely a contractor.

✓ The Fundamental Test

This looks at whether a contracted person is self-employed or if they are working for someone else. Generally, a self-employed person is in business taking risks to make profits, whereas a person working for someone else is generally only remunerated per hour.

✓ Industry Practice

What is common for your industry? For example, courier drivers and Uber drivers are mostly independent contractors. No hourly rate applies, nor minimum hourly rates.

Withholding Tax on Scheduler Payments

Contractors when employed by third parties or the work provided is listed under Schedule 4 of the Income Tax Act. A contractor who receives a schedular payment needs to complete an IR 330 tax code declaration form and give it to the person paying. Note, recruitment agencies are now required by Inland Revenue to deduct tax from contractors at source before it is paid out to the contractor. The contractor needs to complete an [IR330c](#) form and nominate a level of tax deduction

What rate should I charge as a contractor?

This will depend on a number of factors:

- The length of the contract. Short term contracts may justify a higher hourly than longer term contracts.
- The scope of the assignment. Depending on the nature of the assignment where there is currently high demand, your hourly rate may increase. Be prepared to be flexible as you may go through a period of low demand or the work may be seasonal.
- Your track record, qualifications. Reputation and experience in the industry.

Avoid simply dividing your salary by the number of hours you work each year as many do or you will be under paying yourself. As a general guide, use the formula calculating your base salary + 35% (of your base salary) divided by 2000 hours to arrive at an hourly rate This is calculated to cover

- Sick leave
- Annual leave
- Public holidays
- Uncertainty
- Home office expenses, professional and software subscriptions, Xero, Zoom, vehicle costs, car parking, travel etc
- Accounting expenses for compliance with tax obligations (GST, Income Tax, Accounts)
- Professional indemnity and public liability

Remember, these figures are just indicative and rates may vary by region and due your reputation in the industry. Feel free to ask those in the industry to confirm industry norms.