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Independent Contracting Arrangements

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Abstract

On 1 March 2007, the new federal Independent Contractors Act 2006 (Cth) (IC Act) came into force. The principal significance of this legislation is that engagers of labour will be able to take on staff on independent contracts, without concern that any State laws will affect the wages or general working conditions of those whom they engage.

This paper moves forward, and focuses on issues of concern to those enterprises that decide to engage labour as contractors. In particular, we focus on two important questions. First, are your contractors really contractors? (If not, you face the risk of prosecution under new 'sham arrangements' provisions in the WR Act). Second, what do you need to know about terminating the engagement of contractors? It is not enough to put a harsh 'termination on one hour's notice' provision in a written contract. Contractors do have the benefit of new unfair contracts provisions, so we need to consider how those provisions, and other legal principles, may affect termination issues.

University of New South Wales
Faculty of Law
Continuing Legal Education

Employment Law – Working with Work Choices

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Independent Contracting Arrangements

Joellen Riley*

SYNOPSIS OF PRESENTATION

Independent contracting after *Work Choices*

Sometime between now and 11 June 2007, the new federal *Independent Contractors Act 2006* (Cth) (IC Act) will come into force.[1] The principal significance of this legislation is that engagers of labour will be able to take on staff on independent contracts, without concern that any State laws will affect the wages or general working conditions of those whom they engage.[2]

General freedom to employ staff on independent contracts had already been secured by certain provisions of the *Workplace Relations Act* 1996 (Cth) (WR Act), as amended by the *Workplace Relations Amendment (Work Choices) Act 2005* (Cth) (*Work Choices*). Since 27 March 2006, WR Act s

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[1] *The Independent Contractors Act 2006* (Cth) (IC Act) received royal assent on 11 December 2006. The bulk of the IC Act's provisions are to take effect on proclamation, or no later than six months after assent.

[2] The IC Act will apply to all 'constitutional corporations', but not to unincorporated partnerships or sole traders: see IC Act s 5. State laws concerning 'workplace relations matters' will no longer apply to such employers. Be warned, however, that a number of State laws continue to apply, for example, workers' compensation and occupational health and safety matters: see IC Act ss 7-8. For a brief explanation of these sections, see Riley, Joellen 'A Fair Deal for the Entrepreneurial Worker? Self-employment and Independent Contracting Post *Work Choices*' (2006) 19(3) *Australian Journal of Labour Law* 246-262.

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515(1)(g) has explicitly clarified that industrial awards cannot contain any clause restricting employers' choice to engage as many staff as they wish as contractors, nor impose any restrictions on the conditions that can be applied to their engagement. This means that it is impossible in an award to require an employer to pay the same rates or offer the same conditions to contractors or labour hire workers as are provided to employees.

It is now also impossible to include any such restriction in a workplace agreement made under WR Act Pt 8. Restrictions on forms of engagement are one of the many matters listed as "prohibited content" in the *Workplace Relations Regulations (*WRR*).*[3] So employers wishing to avoid the requirements of what remains of industrial awards and any pre-reform certified agreements, and indeed who want to escape regulation by any aspect of the WR Act (including the new Australian Fair Pay and Conditions Standard which mandates certain wages, hours and leave entitlements), might elect to engage labour predominantly by independent contracts, and can do so without having to tolerate any protected industrial action over the matter by unions.

Whether employers will choose this path is still a matter of speculation. An earlier presentation in the UNSW Continuing Legal Education Employment Law series canvassed this issue.[4] This paper moves forward, and focuses instead on issues of concern to those enterprises that decide to engage labour as contractors. In particular, we focus on two important questions:

- Are your contractors really contractors? (If not, you face the risk of prosecution under new 'sham arrangements' provisions in the WR Act); and
- What do you need to know about terminating the engagement of contractors? It is not enough to put a harsh 'termination on one hour's notice' provision in a written contract. Contractors do have the benefit of new unfair contracts provisions, so we need to consider how those provisions, and other legal principles, may affect termination issues.

[3] See WRA s 356 and WRR reg 8.5(1)(h).

[4] See Riley, Joellen "Employees or contractors? Engaging staff following Work Choices, and in the light of the proposed Independent Contractors legislation", *Employment Law – What Choices?* UNSW Faculty of Law CLE, 6 December 2006, Sydney.

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Who is, and who is not, a genuine contractor?

Two aspects of the new package of independent contractor legislation make it clear that pre-existing common law tests for determining the boundary between a "contract of service" (an employment contract) and an independent "contract for services" continue to apply, and continue to mark out important differences in the treatment of workers.

The first of these aspects is the wording of the IC Act s 3(2), which holds that "the rights, entitlements, obligations and liabilities of parties to services contracts" are to be governed "by the terms of those contracts, subject to: (a) the rules of common law and equity as applying in relation to those contracts . . ." Those common law rules include the tests applied in a body of case law, marking out the boundary between services contracts, and employment contracts.[5] The definition of a services contract in s 5 of the IC Act is not at all illuminating, and neither is the definition in s 4 of "independent contractor" which simply says "*independent contractor* is not limited to a natural person". Reliance on the common law tests is consistent with the recommendations of the majority in the *Making It Work* Report of the government's earlier enquiry into independent contracting and labour hire arrangements.[6]

The second aspect of the new laws which demonstrate continued reliance on the common law tests are the new 'sham arrangements' provisions inserted as a new Part 22 of the WR Act by the *Workplace Relations Legislation Amendment (Independent Contractors) Act 2006* (Cth). This Act – a companion to the IC Act – also received assent on 11 December 2006, and will come into force immediately after proclamation of the IC Act. These provisions (set out in more detail below) also depend on the common law distinction between a contract of employment and an independent

[5] For a detailed critical analysis of the common law see Andrew Stewart 'Redefining Employment? Meeting the Challenge of Contract and Agency Labour' (2002) 15 *Australian Journal of Labour Law* 235.

[6] House of Representatives Standing Committee on Employment, Workplace Relations and Workforce Participation, *Making it work: Inquiry into independent contracting and labour hire arrangements*, Canberra, August 2005.

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contract, and they create some new penalties for any engager of labour who misclassifies staff.

Sham arrangements – outline of provisions

Section 904

A new s 904 in the WR Act imposes a pecuniary penalty of up to 300 penalty units (currently $33,000) for contravention of any of ss 900, 901, 902 or 903 of the Act. A workplace inspector, a person affected by the contravention, or an organisation of employees (a union) of which the affected person is a member can bring an action for a contravention of any of the provisions in ss 900-903. If a union is acting on behalf of a member, the member must authorise the union to do so in writing: s 904(3)(c).

Actions can be brought before the Federal Court or Federal Magistrates Court, and the orders available to the court, in addition to penalties, include injunctions and other orders to stop a contravention or remedy its effect. This includes orders to reinstate or reemploy a person, or to order compensation for loss: s 904(2B).

Section 900

Section 900 provides that a person contravenes s 900(1) if the person who is a party to a contract with an individual worker represents to the worker that the contract is a contract for services (i.e., an independent contract), when the contract is in fact an employment contract. A note to sub-s 900(2) states that employment has its "ordinary meaning" in this provision. It is not a contravention, however, if the person who made the representation can prove that they did not know that the contract was a contract of employment, and was not reckless as to whether it was an employment contract. (It is interesting that the wording of the Act differs from that of the initial Bill. In the Bill, an engager would be innocent of a contravention if they "could not reasonably have been expected to know" the contract was really an employment contract. This requirement of objective reasonableness has

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been replaced by a test of actual knowledge or wilful blindness (recklessness).

Section 901

Section 901 makes a similar provision in respect of an offer of engagement. It is a contravention to misrepresent an offer of work as an offer of a contract for services, if it is really an offer of employment. The same excuse is allowed for ignorance, so long as the ignorance was not "reckless".

Section 902

Section 902 prohibits an employer from dismissing, or threatening to dismiss, an employee, if the "sole or dominant purpose" of the dismissal is to re-engage the worker as an independent contractor to do the same or substantially the same work. Section 902(3) provides for a reversed onus of proof – the employer is taken to have dismissed the worker for the sole or dominant reason of re-engaging as a contractor unless the employer can prove otherwise. The reversed onus does not, however, apply in the case of an application for an interim injunction.

The wording of s 902 reflects the freedom of association provisions in ss 792(4), 793(1)(i) and 809 of the WR Act, which create a remedy for an employee who is dismissed for the "sole or dominant" reason that they are entitled to the benefit of a particular industrial instrument (eg, an award or workplace agreement). The "sole or dominant" reason requirement was a Work Choices amendment, no doubt enacted to address the inconvenience created by such decisions as *Greater Dandenong City Council v Australian Municipal Clerical and Services Union*.[7] In that case a council was held to have breached the freedom of association provisions when they put certain work out to tender, because they accepted a lower tender than the one offered by a consortium of former employees who submitted a tender priced to allow them to maintain their existing wage rates. Under the post Work Choices provisions, it is arguable that an employer in such a position could argue that an overall business reorganisation strategy justified their decision,

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[7] (2001) 112 FCR 232.

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and it was not for the sole or dominant reason of reducing employees' wages. An employer faced with a decision about outsourcing work to contractors instead of maintaining an employed workforce would be put to the same kind of test, under these new provisions.

Section 903

While s 902 prohibits dismissals and threats of dismissal, s 903 attacks more subtle conduct. A person contravenes s 903 if they make a statement to an employee or former employee which they know to be false, with the intention of persuading or influencing the employee or former employee to perform the same work as an independent contractor.

The common law boundary

As has been noted above, one of the most important legal issues of concern to independent contractors and those who engage them has not been explicitly addressed in the statute. There is no statutory definition of an independent contract. The statute (like the WR Act) relies entirely on the common law (and hence the judiciary deciding cases on their own facts) to distinguish between a contract for service and a contract of services.[8]

This decision suggests that the government is content to allow the courts to continue to influence the development of this difficult area of law. It also suggests that the government has consciously chosen not to go down the route of duplicating the tests for contractor status adopted in income tax legislation. In the *Making it Work* report, the majority recommended that the common law test for what constitutes employment be maintained,[9] but that it be supplemented by provisions adopting a similar approach to that used in the *Income Tax Assessment Act* 1997 (Cth) (*ITAA*).[10]

The Personal Services Income approach used in the *ITAA* to ensure that independent contracts are not used to avoid liability to make PAYG tax

[8] See *Stevens v Broddribb Sawmilling Co Pty Ltd* (1986) 160 CLR 13; *Hollis v Vabu Pty Ltd* (2001) 207 CLR 121; *Sweeney v Boylan Nominees PtyLtd* [2006] HCA 19 (16 May 2006).
[9] See *Making it Work* above n.6, Recommendation 2 at par [4.48].
[10] See *Making it Work* above n.6, Recommendation 3 at par [4.48].

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deductions uses a number of tests to ensure that the putative independent business person is not in fact a disguised subservient worker, who the government believes ought to be paying tax continuously.[11] These tests include the results test, which asks whether the worker is paid at least 75 per cent of income to produce a result, supplies equipment, and is liable to rectify faults; and the 80 per cent rule, which asks whether more than 80 per cent of income derives from a single client, whether there are at least two unrelated clients, whether at least 20 per cent of work is delegated to others, or whether the putative independent contractor operates from business premises other than home or the place of business of the enterprise contracting for the labour.

The common law approach to distinguishing a contract for services from employment involves weighing in the balance a more extensive and more flexible list of factors. These factors include:

Control: Who dictates hours of attendance? Who dictates not only what is to be done, but how to do it?

Capital/labour contribution: Who provides the capital outlays to support the work? This includes premises and equipment. If a worker provides nothing but their own labour, this factor will weigh in favour of a finding of employment.[12]

Who sets the price? Is there any negotiation over rates of remuneration? Does the worker have any opportunity to turn a profit by managing the enterprise more efficiently?

Delegation: Is the worker genuinely entitled to delegate some or all of the work to others?[13]

This is by no means an exhaustive list. Which factors are most important, and how they are weighed, is very much a matter determined by the particular circumstances of the case.

The High Court of Australia has considered these factors most recently in *Sweeney v Boylan Nominees Pty Ltd.*[14] This case, like the High Court

[11] See ITAA Part 2-42; Div 87.

[12] See for instance the distinction drawn between the bicycle couriers and the motor vehicle couriers in the cases of *Hollis v Vabu Pty Ltd* (2001) 207 CLR 121 and *Vabu Pty Ltd v Federal Commisioner of Taxation* (1996) 33 ATR 537.

[13] See for example *Sammartino v Mayne Nickless t/as Wards Skyroad* (2000) 98 IR 168.

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authority on this subject most recently preceding it *(Hollis v Vabu Pty Ltd),* concerned the vicarious liability of an engager of labour for the torts committed by the worker. While these cases are certainly authority for the general principles to be applied, some decisions of courts below the High Court offer examples of cases more likely to arise in the context of the application of the IC Act and the sham arrangements provisions in the WR Act. Two are worth exploring here. One is the Federal Court decision in *Damevski v Giudice*[15] and the other is *Country Metropolitan Agency Contracting Services Pty Ltd v Slater*[16]*,* a decision of the Workers Compensation Tribunal of South Australia. Both decisions concerned workers who were purportedly engaged as independent contractors, and in both cases, the relevant court found there to be an employment relationship, despite contract documents asserting otherwise.

Damevski v Giudice

This case concerned an employed cleaner who was persuaded to formally resign, but to agree to do his usual job ostensibly as a contractor to a labour hire organisation. Mr Damevski was presented by his employer, Endoxos, with instructions to resign his job and sign an agreement to be engaged by a labour hire entity called MLC Solutions. Mr Damevski never had any direct dealings with MLC. He continued to wear Endoxos' livery, to take instructions as to his work from Endoxos' managers, to submit time sheets to Endoxos, and to rely on equipment provided by Endoxos to do his work. He was told at the time he was required to sign the deal that 'nothing would change'. When Endoxos decided that it no longer needed his services, an Endoxos manager fired him, without consulting MLC Solutions.

Although the AIRC (a single Commissioner and a Full Bench on appeal) were persuaded that the written contract with MLC Solutions determined the matter and that Mr Damevski had no standing to bring an unfair dismissal claim, a Full Court of the Federal Court of Australia

[14] (2006) 227 ALR 46; 152 IR 317; 80 ALJR 900. For a note on this case, see Rolph, David "A Carton of Milk, A Bump on the Head and One Legal Headache: Vicarious Liability in the High Court of Australia" (2006) 19 *Australian Journal of Labour Law* 294.
[15] (2003) 202 ALR 494.
[16] (2003) 124 IR 293.

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disagreed. Applying a reality check to all of these arrangements, the Court found that that the purported labour hire arrangement between Endoxos and MLC solutions represented nothing more than a decision by Endoxos to outsource a payroll function. This case would seem on its face to be an example of a sham arrangement – although even here, it is possible that an employer in Endoxos' position might seek to rely on legal advice to claim a genuine and not "reckless" belief that Damevski was no longer an employee.

Country Metropolitan Agency Contracting Services Pty Ltd v Slater

Ms Slater was a labour hire worker, engaged by Country Metropolitan Agency Contracting Services Pty Ltd (CMACS), and placed with Chiquita Brands Adelaide Pty Ltd to pick tomatoes. She was injured while tomato picking, and her workers compensation claim raised a preliminary question: was she an independent contractor or an employee of CMACS? The hiring agreement between CMACS and Ms Slater had adopted the template used in *Building Workers Industrial Union of Australia v Odco Pty Ltd*,[17] and purported to characterise Ms Slater's engagement as an independent contract. Notwithstanding the terms of this written document, the court held that Ms Slater was an employee.

The factors which influenced this decision included the following:[18]

- She did not supply any equipment of her own, apart from her gardening gloves. In fact, she supplied nothing but her own labour.
- She worked regular hours and was told when to start work and when to finish; what work to do, and how to do it. In this respect, she was obliged to complete time book entries, and she was paid by the hour.
- She was not entitled to delegate work to others.
- She did not provide any skilled labour. She had no special qualifications.

The fact that it was the host business (Chiquita) who gave her instructions and supplied the equipment she used did not defeat a finding that

[17] (1991) 29 FCR 104; 37 IR 380.
[18] 124 IR 293 at 299.

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the labour hire company was her employer. The court held that Chiquita's entitlement to issue those directions arose out of the terms of the contract between CMACS and Ms Slater. She accepted Chiquita's directions, as a consequence of her obligations as an employee of CMACS.[19]

The terms of the written contract between CMACS and Ms Slater were of little weight in the light of the facts of her engagement. She was paid a very low hourly rate: $8.23 per hour while training and $9.20 thereafter. She had no scope to bargain over her rate: it was a "take it or leave it" proposition. She was, in fact, a subjugated casual employee, not an independent contractor, despite the wording of the contract.

These cases, and decisions like them, demonstrate that the IC Act is unlikely to usher in a new world where every worker can be classified as an independent contractor for the purpose of avoiding employment law obligations. Where the worker is a lowly paid, unskilled worker paid a take-it-or-leave-it hourly rate for labour only, it is most unlikely that the worker will be found to be an independent contractor, no matter what form of words are used in the document establishing the engagement. The new sham arrangement provisions in the WR Act increase the risk that an employer seeking to use such stratagems will face trouble. Prior to the IC Act, the worst outcome for an employer using a strategy like this would be that it was not successful. The employer would continue to be liable to pay award wages, or recognise unfair dismissal rights. Now there is the additional risk of a fine under the WR Act for misrepresenting the status of the worker.

Termination issues

A second issue – unaddressed by the new legislation in anything but an indirect way – is the question of termination of independent contracting arrangements. A genuine independent contractor will not have any entitlement to pursue an unfair or unlawful termination remedy under the WR Act, or under any State statute. However it is possible that precipitate termination of an independent contracting arrangement may give rise to

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[19] Ibid at 300.

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complaints under the IC Act's unfair contracts provisions, or possibly even raise a regular, common law contract claim. (This of course will depend upon the resources available to a complainant to mount litigation. Complaints of this nature will now come before courts, not industrial relations tribunals.)

Let us imagine two scenarios. In the first, the engager of labour is using a standard form contract, which states that the contract can be terminated at an hour's notice. In the second, the engagement is much less formal. Either there is no documentation, or the documentation created upon the establishment of the relationship has been so comprehensively ignored in the course of the ensuring relationship that a court finds the real contract between the parties is an unwritten one.[20] We will consider the first scenario in the light of the unfair contracts provisions now in the IC Act, and the second in the light of general commercial law principles.

Unfair contracts provisions

The WR Act has contained unfair contracts provisions for some time now. Prior to the enactment of the Work Choices Act these were contained in ss 127A to 127C. Work Choices redrafted these provisions as ss 832-834. These provisions applied only to independent contracts between constitutional corporations and contractors who were natural persons. Following the passage of the IC Act and its companion legislation, these provisions were repealed and re-enacted in the IC Act.[21] Now they extend to cover contractors who have incorporated their businesses, so long as the work performed under the allegedly harsh or unfair contract is performed by a director of the contractor company or a family member of the director.[22]

Arguably, a contract which allows termination of a long term full-time labour engagement on one hour's notice is palpably unfair according to any ordinary conception of fairness, especially if the worker has been required to provide his or her own equipment, and invest some capital in the arrangement. Would such an arrangement be relevantly 'unfair' or 'harsh' within the terms of the new statutory provisions?

[20] See for example the finding in *Quinn v Jack Chia (Aust) Ltd* [1992] 1 VR 567.
[21] IC Bill Pt 3.
[22] IC Bill cl 11.

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In determining this question, the court is empowered to take into account the matters listed is s 15 of the IC Act. These include the "relative bargaining positions of the parties" (15(1)(a)); and also "whether the contract provides total remuneration that is, or is likely to be, less than that of an employee performing similar work". If the contractors hourly remuneration is the same or not much more than an employee's would be, the lack of the statutory minimum notice period under WR Act s 661 may in itself be sufficient to cause the total remuneration of the contractor to fall short of an employee's remuneration, especially if the contractor has been long serving.

Also, the Court is empowered to consider "any other matter that the Court thinks is relevant", which would appear to leave scope for the Court to develop its own jurisprudence on the fairness of notice provisions in independent contracts.

Common law principles

In developing such jurisprudence, it is arguable that the Court may draw on principles already developed in commercial law. These principles include an emerging principle that commercial contracts must be performed "in good faith". A number of commercial cases have interpreted this obligation to preclude capricious and arbitrary termination of a long-standing relationship on short notice.[23]

Even without recourse to a principle of good faith, it is well established that a commercial relationship for an ostensibly indefinite period can be terminated on "reasonable notice", and that reasonable notice takes account of a number of factors. In *Crawford Fitting Co v Sydney Valve & Fittings Pty Ltd*,[24] the NSW Court of Appeal held that these factors included consideration of the time it would take for the contractor to deploy his or her labour and equipment in alternative employment. In an appropriate case, it would also include a sufficient time to enable the contractor to recoup any extraordinary expenditure sunk into the now terminated project. If a Court were to take the

[23] See *Burger King Corp v Hungry Jack's Pty Ltd* [2001] NSWCA 187 (21 June 2001). See generally Peden, Elisabeth *Good Faith in the Performance of Contracts*, LexisNexis Butterworths, Sydney 2003.
[24] (1988) 14 NSWLR 438.

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view that the relationship between the parties was not governed by any express terms, these are the principles that would apply.

A court may take the view that express terms did not govern a relationship if the parties relationship had already evolved and changed beyond the terms of an earlier document (as in *Quinn v Jack Chia*), or if the notice provision in a written document was contradicted by more specific representations made during negotiations. This was the finding of a full bench of the Federal Court in *Walker v Citigroup Global Markets Australia Pty Ltd*.[25] In that case, a representation that an appointment was for at least a year was held to override the standard one month termination clause in a written document.

As was noted above, the IC Act s 3 provides that principles of contract law and equity continue to apply to contracts falling with the scope of the IC Act. Section 3 goes on to provide that Commonwealth statutes, and State statutes governing commercial laws will also continue to apply to independent contracting arrangements. These contemporary developments include the recognition of principles of good faith in the performance of contracts, the development of equitable doctrines around the concept of unconscionable dealing,[26] and statutory provisions enforcing obligations of fair dealing. For example, the *TPA* and complementary Fair Trading statutes passed in each of the States have radically influenced Australian contract law.[27] The present Chief Justice of Australia, Murray Gleeson, has written (extra-judicially) that:

> [F]or a number of reasons, some to do with the work of legislatures, some to do with judicial law making, and some to do with the temper and spirit of the times, we can no longer say, in all but exceptional cases, the rights and liabilities of parties to a written contract can be discovered by reading the contract.[28]

It seems tolerably clear that the IC Act and its companion legislation, while enabling greater use of contracting arrangements, do not of themselves

[25] [2006] FCAFC 101 (23 June 2006) at [77].
[26] These include as doctrines of estoppel, and unconscientious or unconscionable dealing.
[27] See D Harland "The Statutory Prohibition of Misleading and Deceptive Conduct in Australia and its Impact on the Law of Contract" (1995) 111 *LQR* 100.
[28] Gleeson, M "Individualised Justice – the Holy Grail" (1995) 69 *ALJ* 421 at 428.

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restrain the development of principles of good faith and fair dealing in work contracts. That development is left squarely in the hands of the courts.

Transitional provisions

Engagers of labour intending to make use of the IC Act need to be aware that the Act contains comprehensive transitional provisions which effectively preserve existing independent contract arrangements, unaffected by the exclusion of State laws, for up to three years after proclamation. Parties will be at liberty to renegotiate their arrangements under the federal provisions before the conclusion of the transition period, but this will need to be done consensually. Existing contracts (and this includes arrangements for a rolling series of contracts) cannot be terminated unilaterally, without attracting the sanctions currently available under any applicable State law.[29]

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[29] See Part 5.

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