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UP FOR A GIG? THE RISKS OF WORKER MISCLASSIFICATION IN THE "GIG ECONOMY"

Several "gig economy" business models have sprung up in Malta over the past few years. Cab-hailing services, outsourcing platforms and courier delivery services, to name a few, have adopted the model of engaging with independent contractors for engagements, rather than undertake the orthodox, and admittedly more bureaucratic, route of hiring employees to perform those tasks.

Any undertaking looking to establish operations in Malta should, however, be careful about designing a business model around "independent contractor" arrangements before taking full account of the Maltese law rules governing the correct classification of such workers as employees, regardless of their contractual designation.

In this piece we will consider the critical question: when is a freelancer treated as an employee in terms of Maltese law?

GETTING THE BASICS STRAIGHT

For the purposes of Maltese law, workers are classified either as "employed" or "self-employed":

- **Employees** are individuals who are formally engaged by their employer, typically governed by an employment contract or a letter of engagement setting out the terms of employment. Such relationships enjoy the full protection provided by Maltese and European employment rules;
- **Self-employed workers** are those individuals whose principal source of income is derived from work generated on their own account, and not on the basis of any contractual arrangement with an employer. Such workers typically contract with their customers on the basis of a contract, engagement or arrangement governed by the general civil law, but are not granted the protection of employment law given the absence of any employer-employee relationship.

There are however scenarios where these basic distinctions may be somewhat blurred, as would be the case where employers deliberately identify human resources and engage each resource as a freelance contract for the performance of a specific task or tasks, with the intention of avoiding the costs, obligations (including vacation leave, maternity leave

and sick leave amongst others) and potential risks and liabilities that could arise from the employer-employee relationship. In order to address such abuse, in 2012 the Employment Status National Standard Order (S.L. 452.108) was introduced, setting out an objective test intended to assess and determine whether or not a specific relationship should be correctly classified as one of employment, with all the legal, tax and social security implications that it brings.

THE TEST

The key provision on the Employment Status National Standard Order is Regulation 3, which provides the criteria forming the basis of the test. Essentially, if the relationship between the individual contractor and the recipient of the service meets five or more of the following eight criteria, then the relationship is presumed to be one of employment for the purpose of Maltese law:

1. The contractor depends on one single person for whom the service is provided for at least 75% of his income over a period of one year;
2. The contractor depends on the person for whom the service is provided to determine what work is to be done and where and how the assigned work is to be carried out;
3. The contractor performs the work using equipment, tools or materials provided by the person for whom the service is provided;
4. The contractor is subject to a working time schedule or minimum work periods established by the person for whom the service is provided;
5. The contractor cannot sub-contract his/her work to other individuals;
6. The contractor is integrated in the structure of the production process, the work organisation or the company's or other organisation's hierarchy;
7. the person's activity is a core element in the organization and pursuit of the objectives of the person for whom the service is provided; and
8. The contractor carries out similar tasks to existing employees, or, in the case when work is outsourced, he performs tasks similar to those formerly undertaken by employees.

Very often, freelance arrangements would satisfy three or four of the criteria, with some other criteria being debatable. Such scenarios clearly make the situation unclear, creating a degree of risk for the recipient of the service.

The most noteworthy case is **Albert Falzon vs Melita Mobile Ltd** (Industrial Tribunal Dated 6th November 2014 and Court of Appeal Dated 30th January 2017), which was brought before the Industrial Tribunal alleging a change in employment status. Mr. Falzon was engaged through a contract which stipulated that he was to be considered self-

employed and he received a notice of termination informing him that the period of engagement was expiring.

When the Employment Status National Standard Order came into force, it required employers to provide persons being classified as employee in terms of the said Order with a letter of engagement within eight weeks of its coming into force. The defendant company never sent this letter to Mr. Falzon, and Mr. Falzon referred the matter to the Tribunal to seek a declaration that the employment relationship had been changed from one of a self-employed status to one of indefinite term employment.

The Tribunal considered the facts of the case and applied them to each of the criteria set out in the Order, concluding that Mr. Falzon satisfied criteria (b), (d) and (e). The tribunal noted, however, that the five criteria required by the Order had not in fact been satisfied and thus there was no resulting indefinite employment relationship existing between the parties. Mr. Falzon appealed the decision, and the Court of Appeal confirmed the Tribunal's decision on the same basis.

In order to avoid uncertainty and provide businesses with a "safe harbour", the Order provides that a contractor or a recipient of such service may request the Director of Labour to exempt specific relationships from being construed as employer- employee relationships, provided that the Director is of the view that particular grounds exist to justify the exemption, including arrangements where the activity being carried out is an uncommon occurrence or one of a very short duration.

THE IMPORTANCE OF GETTING IT RIGHT!

The legal, tax, VAT, social security and administrative treatment of an employer-employee relationship is completely different to that subsisting between a contractor and the recipient of that contractor's service.

Thus, for instance, an employment relationship must be covered by an employment contract or by a letter of engagement setting out the terms of employment, and the employment position registered with the Government agency for employment, JobsPlus.

Social security contributions due under a Maltese employment arrangement are borne by the employer and the employee in equal portions between them (at the rate of approx. 10% of the salary- with a maximum total contribution of Eur 93.06 per week, based on 2019 rates). Such contributions are withheld by the employer and settled periodically with the Commissioner for Revenue. The employee's personal income tax is deducted by the employer at source (at the local staggered tax rates, which depend on the amount earned) and similarly settled periodically with the Commissioner for Revenue. Therefore, the employee would receive a net salary, after social security and tax deductions are duly withheld and accounted for by the employer. In the context of an employer-employee relationship, employees are not required to issue any VAT or other fiscal invoice to cover their employment income, and therefore wages so paid by the company are VAT-free.

In the case of individual freelance contractors, each of these considerations is treated differently. Freelancers are registered with the government employment agency, JobsPlus, as “Self-Employed”. They are liable to pay their social security contributions in full (calculated at approximately 15% of the salary payable with a maximum total contribution of Eur 69.79 per week, based on 2019 rates), and also account directly to the Commissioner for Revenue for personal income tax (at the same staggered tax rates that employees pay), but with the liability to pay provisional tax in March, August and December each year. A proper VAT analysis would also be required for freelance activities, and appropriate registration effected with eth VAT authorities. If the contractor provides services for a value of Eur 20,000 or less per annum, he/she may apply for a “VAT exempt” status, meaning that he/she will not need to impose VAT on the sales effected, but will also be unable to deduct any of the input VAT incurred in the course of his/her activities. If the threshold is exceeded, disqualifying the freelancer from the exempt status, or if the freelancer opts for a regular VAT registration, Maltese VAT at the applicable rate of 18% will need to be added to the service provided, and VAT returns submitted periodically (typically quarterly or monthly) to the Commissioner for Revenue, creating an added administrative burden for the freelancer.

RISK? WHAT RISK?

The risk faced by the recipient of a service provided by a freelance contractor is material and significant. The Employment Status National Standard Order provides that any person performing services as a self-employed person for another person, and which are found to fall within the employer-employee results in the contractor being treated as an employee on an indefinite contract of employment, with all the rights and protections that such a status brings.

For the recipient of the service, this is a game-changer, making the recipient liable for social security, the withholding of the contractor’s income tax contributions and a host of other obligations in its capacity as employer.

With this in mind, it certainly is advisable to assess the facts of each particular arrangement carefully and look before you leap. The implications of getting it wrong far outweigh the costs of getting it right!

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