

ACCOUNTING FOR ENTITLEMENTS - CASUAL EMPLOYEES

A JOINT PUBLICATION FROM:



Australian
Institute of
**Company
Directors**



ACCOUNTING FOR ENTITLEMENTS THAT MAY ARISE FOR REGULAR AND SYSTEMATIC CASUAL EMPLOYEES

On 20 May 2020, the full Federal Court of Australia handed down a decision about casual employment classification in **WorkPac Pty Ltd v Rossato** [2020] FCAFC 84 ("Rossato"), which, along with the 2018 case of **WorkPac Pty Ltd vs Skene** ("Skene"), dealt with the circumstances in which employees engaged as casuals may be reclassified as permanent employees, giving rise to a right to retroactively seek entitlements attached to permanent employment, including paid leave benefits. These cases also dealt with the question of whether casual loading paid to the reclassified employees could be offset against historical leave accruals arising out of reclassification. In both cases, it was found that, employees who were currently regarded by an employer as 'casual', but whose employment circumstances otherwise reflected key characteristics of a 'permanent' employee should not have been treated as 'casual'. Further, the Court found that the offsetting provisions that the employer sought to allow them to net casual loading against unused leave entitlements (such as paid annual, public holiday, personal/carer's and compassionate leave) could not be used to offset historical liabilities. Exposure in respect of employees who were engaged in similar circumstances to Rossato or Skene, may extend to a claim for accruals in respect of the period of service for current employees (or otherwise for up to six years following cessation of any employment).

An analysis of the Rossato case included in **Appendix II** below by legal firm Clayton Utz provides a broad overview of the case and some key considerations to be taken into account when determining its applicability to an entity's circumstances.

As a result, for balance dates ending 30 June 2020 and thereafter, affected employers may have an additional remuneration obligation towards some casual employees. Whether an employer has misclassified its casuals is ultimately a matter for legal advice, given that both Rossato and Skene turn on their facts both in relation to reclassification of casual employees as permanent, and the operation of offset provisions.

WHICH ENTITIES AND EMPLOYEES MAY BE AFFECTED?

Employers that have casual employees who have been engaged in a manner providing for a firm advance commitment of employment (i.e. stable, regular and predictable employment), particularly over an extended period of time, may be at risk of exposure to casual misclassification costs. This exposure particularly relates to current casual employees and those engaged in the last six years.

WHAT FACTORS SHOULD BE CONSIDERED TO DETERMINE WHETHER AN ENTITY HAS AFFECTED EMPLOYEES (CURRENT AND FORMER)?

According to Clayton Utz, in order to assess whether casual employees might be classified as permanent employees at law, considerations would include the following (noting that some of these items, below, would not necessarily suggest a non-casual engagement, affirming that it is important to seek professional legal advice for confirmation):

- review casual staff to determine whether their hours and shifts appear regular and systematic over the course of their employment
- review whether there is a "firm advance commitment" as to the hours or days worked by casual staff
- review whether there is likely to be the expectation of "continuing and indefinite work" on behalf of a casual employee i.e. there have been regular patterns of work, certainty, continuity of work or predictability over a 12-month period
- look at any enterprise agreement, industrial award or contract of employment to see whether casual or permanent employees are defined and to see whether regular or systematic casual employees meet that definition
- determine whether any casual employee has refused shifts or an offer of permanent work, and
- to the extent that an employer may seek to rely upon offset provisions in an employment contract to meet historical liabilities associated with reclassification, it is important to revisit the drafting of those offset provisions post Rossato. The decision in Rossato suggests that common formulations of casual loading offset provisions would not create an effective offset.

The Fair Work Ombudsman issued guidance on determining **different types of employees**. In addition to the information provided in Appendix II below, Clayton Utz published a web page with other **practical steps** to consider for employers who are concerned about the ramifications of the Rossato case.

CONSIDER SEEKING EXPERT ADVICE

The decisions in Skene and Rossato relate to specific instances of advance commitment to work - in particular fly-in-fly-out labour servicing scenarios. The topic of offset considered in these cases is somewhat technical from a contract and industrial law perspective. Rossato is also currently the subject of an appeal to the High Court of Australia. Given the potential impact of these decisions, it is important to consider seeking legal advice before arriving at a view on whether an employer should recognise a potential liability reflecting historical leave entitlements for employees previously regarded as casual.

Where an employer identifies a potential exposure, regard should be had to statutory and award/enterprise agreement entitlements that have accrued on an historical basis, including leave benefits and other entitlements (e.g. casual employees are commonly carved out of certain overtime or penalty rate provisions in award or enterprise agreement terms). Legal advice may also be required in determining how limitation periods should apply in relation to historical liabilities and whether any casual employee should be considered as permanent for all, or only some of their service period for the purposes of determining potential liabilities.

Some matters to consider include:

- Whether the legal circumstances considered in the above cases apply to the entity's employment arrangements (with its casual workforce or some identified casual employees within that workforce).
- To what entitlements any identified (affected) casual employees are eligible. The Rossato ruling concluded that Mr Rossato was entitled to annual leave, public holidays (except Christmas shutdown), personal carer's leave and compassionate leave. Although the Rossato ruling does not consider other entitlements that permanent employees may be entitled to such as long service leave (subject to state-based legislation), redundancy pay etc., an organisation may need to determine the extent of its obligations to affected casual employees. Such entitlements may not only be those relating to statutory or contractual obligations, but also those that may arise from constructive obligations.

ACCOUNTING AND FINANCIAL REPORTING IMPLICATIONS

Affected entities may have a potential obligation for entitlements arising in respect of contractual arrangements with casuals impacted by the recent case law.

Consider whether the legal circumstances in the above cases apply to the entity's own employment arrangements

In practice, affected entities may group employment arrangements with similar characteristics to assess whether the principles arising from the above-mentioned court cases apply. The outcome of such assessments may result in the following:

- The entity's financial statements are affected when:
 - o Legal circumstances from the above cases probably apply (i.e. the entity probably employs or has employed regular and systematic casual employees who may be deemed to be permanent employees), or
 - o Legal circumstances from the above cases possibly (but not probably) apply (i.e. the entity possibly employs or has employed regular and systematic casual employees who may be deemed to be permanent employees).
- The entity's financial statements are unaffected when clearly none of the facts/principles apply (e.g. the entity did not employ casuals, or the prospects of the entity employing or having employed regular and systematic casual employees who may be deemed to be permanent employees is remote).

Consider what entitlements any affected casual employees are eligible for

After determining which groups of employment arrangements are affected, a practical way to assess the financial reporting impacts may be to separately consider each type of affected employee benefit. Some benefits may be required by reference to legal minimums or industry awards and others by reference to the entity's policies (which may result in constructive obligations). For each type of benefit, affected entities may have to:

- Recognise a liability (an accrual or provision) and related expense (or asset in some cases, e.g. where the employee cost would have been capitalised into an asset such as the construction of plant and equipment, or inventory on hand), or
- Disclose a contingent liability.

Entities may therefore need to consider the financial reporting requirements on a benefit-by-benefit basis (for each group of employment arrangements identified). Entities also need to consider the recognition or disclosure implications for associated matters such as taxation (e.g. withholding tax and payroll tax) and superannuation guarantee contribution payments.

Appendix I summarises the various possible financial reporting implications.

The Australian Securities and Investments Commission (ASIC) has published a frequently asked questions (**FAQ 1**) that provides guidance on some of the financial reporting considerations associated with the case law.

The ASIC FAQ states:

Companies should consider whether they should provide for additional employee entitlements (including annual leave, personal and carer's leave, compassionate leave, public holiday pay, and redundancy payments) for past and present 'casual employees' who were employed in circumstances covered by the recent Federal Court decision in WorkPac Pty Ltd v Rossato [2020] FCAFC 84. The decision did not allow an offset for any casual loading paid. While no provision would be required for 'casual employees' who are unaffected by the decision, a provision or contingent liability may be required for 'casual employees' employed in circumstances that were not clearly covered by the decision. Companies may wish to seek legal advice.

The Australian Accounting Standards that may be relevant in considering the accounting implications of the case law are:

- AASB 119 *Employee Benefits* (AASB 119)
- AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* (AASB 137).

AASB 137 sets out the accounting treatment for provisions and contingent liabilities that ASIC refers to in its FAQ. AASB 137 requires AASB 119 to be applied when that standard deals with a specific type of provision or contingent liability, instead of AASB 137. Since it is unclear whether AASB 119 addresses all the potential accounting scenarios that may arise from the case law, various accounting considerations arising from both AASB 119 and AASB 137 are summarised in the table below.

	Case law circumstances probably apply to a group of current or former employees.		Case law circumstances possibly (but not probably) apply. A possible obligation exists.	
	Within the scope of AASB 119 <i>Employee Benefits</i> ¹ (Australian Accounting Standards Board 119)	<ul style="list-style-type: none"> • Not within the scope of AASB 119¹ • A present obligation exists, and the amount and/or timing is uncertain • A reasonable estimate may or may not be possible 		
Application	AASB 119 applies when it is clear that the obligation relates to employee benefits. AASB 119 provides requirements and guidance on recognition, measurement and disclosure relating to that obligation.	<p>AASB 137 <i>Provisions, Contingent Liabilities and Contingent Assets</i> (Australian Accounting Standards Board 137) applies when a present obligation exists, but the amount or the timing of the settlement are uncertain:</p> <ul style="list-style-type: none"> • The past events giving rise to the present obligation are the employment services rendered and the case law. • The entity has no realistic alternative but to settle the obligation created by these events. <p>Note that the outflow of economic resources could be over a period longer than 12 months after the reporting period.</p>	<p>AASB 137 applies when a possible obligation exists whose existence will be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.</p> <p>The provision of services by certain employees is not enough. The entity awaits confirmation of an obligating event (either by law or construct) to confirm that particular benefits are owed to particular employees or group of employees.</p>	
	↓	↓	↓	↓
Accounting treatment	<p>Recognise an accrual at the undiscounted amount of “short-term employee benefits” and an expense to profit or loss (unless another standard requires or permits the inclusion of the benefits in the cost of an asset).</p> <p>For “other long-term employee benefits,” such as long service leave, recognise an ‘expected value’ accrual for past service, even though the benefit may have not yet vested at the end of the reporting period.</p>	<p>In some cases, the entity may not be certain as to the amount (or timing) of the liability. Where the effect of the time value of money is material (due to deferred settlement), the estimate is discounted.</p> <p>Recognise a reliable estimate of the settlement as a provision when the amount can be measured reliably.</p>	Disclose a contingent liability where the amount cannot be measured reliably.	Disclose a contingent liability, unless the possibility is remote.
	↓	↓	↓	↓
Disclosure	See AASB 119, par. 25.	See AASB 137, par. 84-85, 88 and 92.	See AASB 137, par. 86-88 and 91-92.	
	Disclose information on assumptions made about the future, and other major sources of estimation uncertainty , that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year AASB 101 <i>Presentation of Financial Statements</i> (AASB 101, par. 125).		↓	
	Disclose judgements , apart from those involving estimations (see above), that management has made in the process of applying its accounting policies and that have the most significant effect on the amounts recognised in the financial statements (AASB 101, par. 122).			
	↓			
Prior year adjustments	<p>Apply AASB 108 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> (AASB 108). If accounting adjustments are made purely due to the new information provided by the Rossato case, it is likely to be treated as a change in estimate. If adjustments are made due to events or decisions beyond the Rossato case, careful consideration needs to be given to whether there is also a change in accounting policy and/or a prior period error being corrected. It should be noted that prior period errors are omissions/misstatements in financial statements arising from a failure to use, or misuse of reliable information that was available, and could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.</p> <p>The AASB has published an FAQ on the underpayment of wages, which may be helpful when considering the application of AASB 108, but care should be taken as it pertains to an entirely different issue.</p>			

¹See AASB 137, par. 1(c) and 5(d) and AASB 119, par. 2. Please note this guide does not express a view on whether to apply AASB 119 or AASB 137 when the case law circumstances probably apply to a group of current or former employees. The determination will depend on specific circumstances and we have provided the relevant paragraph references from AASB 137 and AASB 119 to assist with the judgement.

APPENDIX II

CLAYTON UTZ

Workpac Pty Ltd v Rossato

What happened in the case?

On 20 May 2020, the full Federal Court of Australia handed down a decision about casual employment classification and leave entitlements. In summary, the Court held that Mr Rossato, who had been classified as a casual employee during his employment by Workpac, was not in fact a casual employee and was entitled to receive permanent employment entitlements in addition to retaining all casual loading payments he had received over the course of his employment.

Mr Rossato was employed as a mining truck driver by a labour hire company for 3.5 years under six consecutive contracts. The contracts identified him as a casual employee and he was paid a 25% casual loading rate. The incorporation of this casual loading rate into his rate of pay was mentioned in three contracts. Mr Rossato received weekly rosters which were often fixed for long periods of time and were established far in advance, sometimes up to seven months. Consistent with the existing common law test, the court said that stable, regular and predictable employment or "a firm advance commitment" of employment will be a primary point of consideration in discerning whether a casual employee is, in fact, a permanent employee. This was found to be made out in this case.

In finding that Mr Rossato was not in fact a casual employee, the court also found that he was able to retain all casual loading payments he had received over the course of his employment, as well as retrospectively recover his accrued and untaken annual, personal and compassionate leave entitlements. The payment of casual loading by WorkPac was found to be ineffective in setting off any payments for untaken and accrued leave that he was later found to be entitled to. This aspect of the decision has given rise to significant uncertainty in the business community with respect to the engagement of casuals.

How to determine whether it applies?

In order to assess whether the Rossato decision presents a real risk for an entity, it is first necessary to understand what a "true casual" is. Unlike part time or full-time employees, casuals have no guaranteed hours. They are employed on an "as needed" basis, generally to provide rostering flexibility and/ or to meet irregular operational demands etc. Casuals must get paid a casual loading on top of their base hourly rate of pay (usually 25%, though this may differ where casuals are covered by an industrial instrument that confers a greater or lesser entitlement), because they do not have the security of employment of permanent staff. Specifically, they have no guaranteed hours of work and no entitlement to annual leave, paid personal / carer's leave, notice of termination or redundancy pay.

Importantly, not all long-term casuals will bring Rossato-type risks. Casuals come in two types. They can be irregular casuals who work inconsistent hours on an irregular basis or they can be regular and systematic casuals who work regular and systematic hours (e.g. same number of hours or on the same day each week) and have an expectation of ongoing work. This does not make them permanent staff, but it does mean that unlike irregular casuals, they have additional rights after 12 months' employment, such as access to parental leave and flexible working arrangements under the Fair Work Act 2009 (Cth) and the ability to bring an unfair dismissal claim if their employment is terminated.

Whether there is a risk of a regular and systematic casual employee being found to be a permanent employee will ultimately rely on the factual matrix of the individual employee (i.e. a court's assessment of whether are they a true casual or a permanent employee?), so it is important not to simplistically conflate long-term regular and systematic casuals with permanent staff in a broad-brush manner, though without doubt such staff are the casuals that present the highest risk.

Where a casual is underpaid they can make a claim for up to six years' back pay from the date the claim is lodged.

In order to assess whether so-called casual employees might be classified as permanent employees at law, entities should:

- review casual staff to determine whether their hours and shifts appear regular and systematic over the course of their employment;
- review whether there is a "firm advance commitment" as to the hours or days worked by casual staff;
- review whether there is likely to be the expectation of "continuing and indefinite work" on behalf of a casual employee i.e. there have been regular patterns of work, certainty, continuity of work or predictability over a 12-month period;
- look at any enterprise agreement, industrial Award or contract of employment to see whether casual or permanent employees are defined and to see whether regular or systematic casual employees meet that definition;
- determine whether any casual employee has refused shifts or an offer of permanent work;
- review whether a casual contract of employment has an appropriately worded set-off clause.

Ultimately this may be a matter on which you require specialist legal advice.

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