

Committee Secretary  
Senate Education and Employment Legislation Committee  
By email: [eec.sen@aph.gov.au](mailto:eec.sen@aph.gov.au)

10 April 2017

Dear Secretary,

**Submission to the inquiry of the Senate Education and Employment Legislation Committee into the Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017**

This submission broadly welcomes the Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017 (Cth). This Bill recognises that there is a serious, and in many cases systemic, problem of non-compliance with labour laws and this affects many vulnerable workers (including migrant workers).<sup>1</sup>

We note that there was a very compressed timeframe for making submissions as part of this inquiry. As a result of these time constraints, we have only had the opportunity to comment on a limited number of the proposed amendments. However, we would be more than willing to elaborate on this submission, or other provisions in the Bill, either in a supplementary submission or in person.

Whilst endorsing key aspects of the Bill, we submit that the Bill should be amended in key respects. We make the following recommendations:

*Recommendation One*

The provisions relating to ‘serious contraventions’ be amended to include breaches of Part 3-1 of the *Fair Work Act* (General Protections).

*Recommendation Two*

In addition to franchise networks and corporate groups, other types of organisational forms (including supply chains and labour hire arrangements) should be captured by Division 4A.

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<sup>1</sup> Senate Education and Employment Committee References Committee, *A National Disgrace: The Exploitation of Temporary Migrant Workers* (2016) 6, 262 (‘Senate Inquiry - A National Disgrace’).

### *Recommendation Three*

To reduce confusion and enhance clarity, the terms 'franchisee entity' and 'responsible franchisor entity' in s 558A should be defined to more closely reflect the definitions of similar terms (such as 'franchise', 'franchisor' and 'franchisee') in the Franchising Code of Conduct.

### *Recommendation Four*

Amendments to section 325 of the *Fair work Act* should be changed to:

- Clarify that a 'requirement' can be imposed through unlawful conduct;
- Elaborate on the meaning of 'unreasonable' as provided under the Explanatory Memorandum to the Bill;
- Remove the requirement of benefit for the employer or a party-related to the employer in relation to 'unreasonable' payments; and
- Extend to prospective employers and employees.

### *Recommendation Five*

Part 4, Schedule 1 of the Bill be amended so that the powers it proposes can only be exercised in relation to workers whose rights under the *Fair Work Act* are suspected to have been breached when there are compelling reasons.

### *Recommendation Six*

- Recommendation 24 of the Senate report, *A National Disgrace: The Exploitation of Temporary Migrant Workers* (2016) should be adopted; or
- The proposal for a new ministerial direction made by Redfern Legal Centre should be adopted.

### *Recommendation Seven*

A 'firewall' should be enacted between the Fair Work Ombudsman and the Department of Immigration and Border Protection that prevents the provision of information by the Ombudsman to the Department in relation to workers who have contacted the Ombudsman.

The analysis behind our recommendations is set out below.

***Schedule 1, Part 1 – Increasing maximum penalties for contraventions of certain civil remedy provisions***

We welcome the amendments relating to ‘serious contraventions’ in order to deal with breaches by employers that are deliberate and systematic. We also welcome the increase in the maximum penalty for breaching the obligations in relation to employee records and pay-slips respectively found in sections 535 and 536 of the *Fair Work Act 2009* (Cth).

These amendments relating to ‘serious contraventions, however, suffer from a shortcoming in that they do not extend to breaches of Part 3-1 of the *Fair Work Act 2009* (Cth) (General Protections).<sup>2</sup> In our view, this is a serious omission. There is clear evidence that the exploitation of migrant workers is *not* restricted to non-payment and under-payment and, in many cases, involves breaches of the rights under Part 3-1 of the *Fair Work Act*, including provisions relating to adverse action and sham contracting.

In relation to adverse action, we note the Fair Work Ombudsman’s report into the Baiada Group found the workers on 417 visas to be subject to discrimination.<sup>3</sup> The Senate report, *A National Disgrace: The Exploitation of Temporary Migrant Workers*, similarly received evidence of discrimination in relation to 457 visa holders.<sup>4</sup> It also documented a contract used by Thies Services Pty Ltd - which considers itself ‘the world’s largest mining services provider’<sup>5</sup> - that allowed Thies to dismiss a worker if ‘engaging in trade union activities’.<sup>6</sup> Recently, a Fairfax expose on the Seasonal Worker Program reported that some of the workers brought under this program were told that ‘(i)f you want to come back (to Australia), you have to leave the union’.<sup>7</sup>

We also note that the sham contracting provisions of the FW Act are not subject to the increased penalty regime relating to ‘serious contraventions’. This is another significant omission given that there is growing evidence of businesses incorrectly classifying employees as independent contractors – either directly or via intermediaries – in a bid to circumvent

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<sup>2</sup> Items 3 to 12, Part 1, Schedule 1 of the Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017 (Cth) (‘Vulnerable Workers Bill’) do *not* amend subsection 539(2) (cell at table item 11, column 4).

<sup>3</sup> Fair Work Ombudsman, *A Report on the Fair Work Ombudsman’s Inquiry into the Labour Procurement Arrangements of the Baiada Group in New South Wales* (2015) 3.

<sup>4</sup> Senate Inquiry - A National Disgrace, above n 1, 153-154.

<sup>5</sup> See <https://www.thiess.com>.

<sup>6</sup> Senate Inquiry – A National Disgrace, above n 1, 154-155.

<sup>7</sup> Nick McKenzie and Nick Toscano, ‘Seasonal Workers Program pickers told if they join a union they’ll get no work’, *The Sydney Morning Herald*, 12 March 2017, <http://www.smh.com.au/business/seasonal-workers-warned-if-they-join-a-union-theyll-get-no-work-20170309-guujgv.html>.

minimum employment standards set by the FW Act (and relevant industrial instruments)<sup>8</sup> including in relation to temporary migrant workers.<sup>9</sup>

Finally, we recognise that the proposed ten-fold increase in maximum penalties is designed to provide an ‘effective deterrent’<sup>10</sup> to potential wrongdoers. In a number of previous articles, we have strongly advocated for a significant uplift in the maximum penalties available under the FW Act on this basis.<sup>11</sup> However, we also note that some of our more recent research on employer behaviour under the FW Act suggests that the relationship between deterrence and compliance is not necessarily straightforward or in line with theoretical expectations.<sup>12</sup> In particular, our research suggests that: ‘[w]e must be wary of falling for the simple fairy tale that higher sanctions lead to greater compliance.’<sup>13</sup> In addition to increasing the available penalties, it is critical (if not more so) to increase the perceived risk of detection. To achieve this aim, it is necessary to ensure that the relevant regulator, the FWO, is sufficiently resourced and supported in seeking out non-compliance and stemming its spread in layers of the labour market which are populated by vulnerable workers. The proposed reforms in relation to record-keeping and investigation powers are vital in this respect.<sup>14</sup>

### *Recommendation One*

The provisions relating to ‘serious contraventions’ be amended to include breaches of Part 3-1 of the *Fair Work Act* (General Protections).

## ***Schedule 1, Part 2 – Liability of responsible franchisor entities and holding companies***

### *General Comments*

The proposal to hold franchisor entities and holding companies responsible for prescribed contraventions of the FW Act occurring within their business networks is an essential and

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<sup>8</sup> See, eg, *Fair Work Ombudsman v Quest South Perth Holdings Pty Ltd* (2015) 326 ALR 470; and Fair Work Ombudsman, *Sham Contracting and the Misclassification of Workers in the Cleaning Services, Hair and Beauty and Call Centre Industries – Report* (November 2011); Fair Work Building and Construction, *Working Arrangements in the Building and Construction Industry* (2012); Brian Howe et al, *Lives on Hold: Unlocking the Potential of Australia’s Workforce* (The Independent Inquiry into Insecure Work in Australia, Australia, 2012).

<sup>9</sup> Senate Inquiry – A National Disgrace, above n 1, 326.

<sup>10</sup> *Ibid.*

<sup>11</sup> See, eg, Tess Hardy, John Howe and Sean Cooney, ‘Less Energetic but More Enlightened? Exploring the Fair Work Ombudsman’s Use of Litigation in Regulatory Enforcement’ (2013) 35 *Sydney Law Review* 565; and Tess Hardy, ‘Who Should be Held Liable for Workplace Contraventions and On What Basis?’ (2016) 29 *Australian Journal of Labour Law* 78.

<sup>12</sup> See, eg, John Howe and Tess Hardy, ‘Business Responses to Fair Work Ombudsman Compliance Activities’ (Centre for Employment and Labour Relations Law, Research Report, January 2017).

<sup>13</sup> Christine Parker and Vibeke Lehmann Nielsen, ‘Deterrence and the Impact of Calculative Thinking on Business Compliance with Competition and Consumer Regulation’ (2011) 56(2) *The Antitrust Bulletin* 377, 415.

<sup>14</sup> See, eg, Schedule 1, Parts 4-6 of the Vulnerable Workers Bill.

appropriate extension of the existing regulatory framework. In particular, Part 2 of Schedule 1 reflects the evolution of work in modern society in that it recognises, at least with respect to corporate groups and franchise networks, that key conditions of employment, and compliance behaviour, may be determined, directly or indirectly, by organisations outside and beyond the putative employer. The proposed reform also recognises that it is no longer acceptable for lead firms, such as franchisors and holding companies, to ‘have it both ways’<sup>15</sup> – to exercise high levels of influence over the performance of work, and yet remain legally insulated from the problems this may create.

We acknowledge that franchising is an important and growing part of the Australian labour market and that there is a great diversity in franchising models and systems across a range of different industries. Further, we do not believe that all franchise networks are constructed, or controlled, in such a way as to promote or permit systemic underpayment of workers. However, over the past 18 months or more, we have witnessed a seemingly endless wave of stories of serious worker exploitation and intimidation in a number of well-known franchises, including 7-Eleven,<sup>16</sup> Pizza Hut,<sup>17</sup> Caltex,<sup>18</sup> Domino’s Pizza<sup>19</sup> and United Petroleum.<sup>20</sup> In our view, the proposed reform represents a positive step forward in terms of addressing the pernicious and persistent problems associated with the recovery of civil penalties and underpayments against firms who seek to evade their employment law responsibilities through the use of corporate vehicles, contractual devices and insolvency. It is clear that the current laws, and voluntary mechanisms, are not working effectively in promoting and ensuring widespread employer compliance with minimum employment standards.<sup>21</sup>

While there are practical advantages and efficiency arguments which support the legal pursuit of lead firms, especially where the direct employer entity is judgment-proof, the ascription of liability to such firms can be normatively justified on a number of other grounds. In our view, making lead firms, such as franchisors and holding companies, liable for employment contraventions is defensible where:

- a) the lead firm has *caused* the direct employer to contravene the law;

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<sup>15</sup> David Weil, *The Fissured Workplace: Why Work Became So Bad for So Many and What Can Be Done to Improve It* (Harvard University Press, 2014).

<sup>16</sup> Fair Work Ombudsman, *A Report of the Fair Work Ombudsman’s Inquiry into 7-Eleven: Identifying and Addressing the Drivers of Non-compliance in the 7-Eleven Network* (April 2016).

<sup>17</sup> Adele Ferguson, ‘Wage fraud: Pizza Hut hit with fines’, *The Sydney Morning Herald*, 27 January 2017.

<sup>18</sup> Adele Ferguson and Mario Christodoulou, ‘Caltex doubles down on wage fraud’, *The Sydney Morning Herald*, 4 November 2016.

<sup>19</sup> Adele Ferguson and Mario Christodoulou, ‘The Domino’s effect: How Australia’s biggest pizza chain has squeezed franchisees while its franchisees have underpaid workers and exploited migrant labour and its investors have made millions’, *The Sydney Morning Herald*,

<sup>20</sup> Adele Ferguson and Sarah Danckert, ‘United Petroleum blasted by Fair Work Ombudsman for underpaying staff’, *The Sydney Morning Herald*, 6 April 2017.

<sup>21</sup> Nick Toscano, ‘Fair Work Ombudsman warns of cutting ties with Domino’s amid wages saga’, *The Sydney Morning Herald*, 2 March 2017.

- b) the lead firm has, directly or indirectly, *benefited* from the contraventions;
- c) the lead firm has power to *prevent* or *deter* workplace contraventions taking place; and/or
- d) the behaviour of the lead firm increases social costs and invites *moral sanction* – this is especially relevant where the lead firm has made public representations that it is committed to ensuring workplace relations compliance throughout its business, supply chain or franchise network.<sup>22</sup>

The FWO's findings in the 7-Eleven Inquiry lend weight to many of these normative justifications. For example, 7-Eleven Stores has vigorously denied that the viability of the 7-Eleven franchise system is (or was) dependent on franchisees underpaying their staff. The FWO also acknowledged that 7-Eleven Stores 'does not directly benefit when a franchisee underpays their workers'.<sup>23</sup> However, the regulator went on to observe that the franchisor gains an indirect benefit from the (often misguided) perception of store profitability in so far as it allows the store to continue to trade and to generate revenue and other fees for 7-Eleven Stores.<sup>24</sup> In addition, the FWO noted, as part of its Inquiry, that 7-Eleven Stores was in a position to prevent workplace contraventions amongst its franchisees, given that it 'controlled the settings of the system in which the franchisee employers operated'<sup>25</sup> and had the resources and capacity to detect and deter franchisee non-compliance. Finally, the FWO found that while 7-Eleven Stores ostensibly promoted compliance with workplace standards, it 'did not adequately detect or address deliberate non-compliance and as a consequence compounded it.'<sup>26</sup> While the 7-Eleven franchise structure is somewhat unique, the issues identified above are not isolated to this particular network. Rather, in our view, similar issues of systemic workplace non-compliance have arisen in other franchise networks, such as Caltex and Domino's Pizza.

The significant legal reform set out in Schedule 1, Part 2 has been welcomed by some, and resisted by others. The FWO has expressed hope that these new laws 'will help to change the attitude of some head franchisors about the investment required'<sup>27</sup> to ensure compliance. However, a recent survey of franchisors found that a majority opposed the introduction of

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<sup>22</sup> See Tess Hardy, 'Good Call: Extending Liability for Employment Contraventions Beyond the Direct Employer' in Ron Levy, Molly O'Brien, Simon Rice, Pauline Ridge and Margaret Thornton (eds) *New Directions for Law in Australia: Essays in Contemporary Law Reform* (ANU Press, 2017, forthcoming). See also Guy Davidov, 'Indirect Employment: Should Lead Companies be Liable?' (2015) 37 *Comparative Labor Law & Policy Journal* 5; and Brishen Rogers, 'Toward Third-Party Liability for Wage Theft' (2010) *Berkeley Journal of Employment and Labour Law* 1.

<sup>23</sup> Fair Work Ombudsman, *A Report of the Fair Work Ombudsman's Inquiry into 7-Eleven: Identifying and Addressing the Drivers of Non-compliance in the 7-Eleven Network* (April 2016) ('7-Eleven Inquiry') 38.

<sup>24</sup> Ibid 39.

<sup>25</sup> Ibid 67.

<sup>26</sup> Ibid 4.

<sup>27</sup> Natalie James, 'Fair Work Ombudsman Address to the Franchise Council of Australia NSW Luncheon (Speech delivered at FCA, Sydney, 1 September 2016).

'joint responsibility' provisions.<sup>28</sup> Bodies representing employers and franchisors, such as Ai Group ('AiG') and the Franchise Council of Australia ('FCA') have strongly argued that holding franchisors accountable for workplace contraventions committed by its franchisees represents a 'regulatory over-reach',<sup>29</sup> which is both unnecessary and unhelpful. More specifically, it has been claimed that the existing laws relating to accessorial liability are sufficient in addressing the relevant issues of franchisee non-compliance.<sup>30</sup> It has been further contended that the vast majority of franchisors are 'small businesses'<sup>31</sup> and shifting the allocation of risk in franchises will 'negatively impact investment, growth and employment'<sup>32</sup> and lead to the demise of the franchise business model.<sup>33</sup> Instead, it has been argued that leveraging ethical, moral or reputational concerns of franchisors would be more appropriate in addressing worker exploitation within franchises.<sup>34</sup> Finally, the FCA, amongst others, have complained that:

the risk of worker underpayment exists across the economy and commercial relationships create a degree of control from one business over another that may impact on Fair Work Act compliance, yet the Government's Bill targets only franchising.<sup>35</sup>

Before considering the proposed provisions in detail, we wish to address each of these points in turn.

First, as noted above, some have sought to argue that existing accessorial liability provisions of the FW Act are 'adequate'<sup>36</sup> in terms of addressing the compliance problems afflicting franchises. In support of this position, they have pointed to the FWO's successful civil remedy litigation against the franchisor of the Yogurberry chain under s 550 of the FW Act.<sup>37</sup> However, it is important to recognise that the circumstances of this particular case are unique and do not necessarily reflect the typical business format franchise arrangement. As such, the

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<sup>28</sup> Lorelle Frazer et al, *Franchising Australia 2016* (Asia-Pacific Centre for Franchising Excellence, 2016) 29.

<sup>29</sup> World Franchise Council Joint Declaration, 'Global franchise community urges Australian sector collaboration to avoid regulatory over-reach', 14 March 2017.

<sup>30</sup> See Lorelle Frazer and Maurice Roussety, 'Franchises shouldn't share responsibilities for stuff ups', *The Conversation*, 16 December 2016.

<sup>31</sup> It is not entirely clear on what basis this claim is being made i.e. on the numbers of employees or on the basis of revenue. See Franchise Council of Australia, 'Submission by the Franchise Council of Australia in relation to the possible amendment of the Fair Work Act to extend liability to franchisors and parent companies in certain situations' (22 November 2016).

<sup>32</sup> Adam Gartrell, 'Bruce Billson spearheads campaign to water down worker exploitation bill', *The Sydney Morning Herald*, 7 April 2017.

<sup>33</sup> Ai Group, 'Fair Work Amendment Bill could discourage investment in franchise businesses' (Media Release, 1 March 2017).

<sup>34</sup> Lorelle Frazer, '7-Eleven fallout: what are the moral obligations on franchisors?', *The Conversation*, 10 September 2015.

<sup>35</sup> Franchise Council of Australia, 'Government's well-meaning on 'vulnerable workers' but misses the mark' (Press Release, 1 March 2017).

<sup>36</sup> FCA Submission 2016, above n 31, 2.

<sup>37</sup> *Ibid*; and Frazer and Roussety, above n 30.

decision is therefore confined to its facts. More specifically, in the Yogurberry litigation, the putative employer entity (i.e. the franchisee which operated the relevant store and employed the Korean backpackers at the time) and the head franchisor were part of a complex group of companies controlled by various members of the same family.<sup>38</sup>

This corporate nexus, overlaid with close family connections, is not generally present in the majority of franchise networks. Indeed, where the franchisee is an independent and separate business and not part of the same corporate or familial group as the franchisor, it is much more difficult to establish that the franchisor had the requisite knowledge of the essential elements of the contraventions. Accordingly, it is much more challenging to use the accessorial liability provisions to seek compensation and penalties against the franchisor.<sup>39</sup> These challenges were laid bare in the FWO's comprehensive inquiry into 7-Eleven. In this inquiry, the FWO found that the company holding the license to the 7-Eleven brand in Australia, 7-Eleven Stores Pty Ltd, 'could have done more, and acted earlier'<sup>40</sup> in curbing employer non-compliance throughout its franchise network. However, the regulator ultimately concluded that it did not have sufficient probative evidence to pursue 7-Eleven Stores under the accessorial liability provisions of the FW Act.<sup>41</sup>

One of the problems facing the FWO in the 7-Eleven instance, and more generally, is that a high bar has been set in relation to satisfying the 'requisite knowledge' requirement under s 550(2)(c) of the *FW Act*, particularly with respect to contraventions of modern awards.<sup>42</sup> In particular, there is a need to establish that the accessory had 'actual knowledge' of the essential elements of the contravention. Actual knowledge is said to include 'wilful blindness' but does not generally encompass 'recklessness or negligence'.<sup>43</sup> Further, constructive knowledge is not sufficient.<sup>44</sup>

In the inquiry report, the FWO observed that a number of individuals employed or engaged by 7-Eleven Stores may have had knowledge of, or capacity to access, essential facts relating to the contraventions committed by the franchisees. However, many of these individuals

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<sup>38</sup> See *Fair Work Ombudsman v Yogurberry World Square Pty Ltd* [2016] FCA 1290 (2 November 2016).

<sup>39</sup> In the latest survey of the franchise sector, it is estimated that the proportion of franchised units held by franchisors was 90 percent. Just over one third of brands (35 percent) are fully franchised, with no company unit ownership. Frazer et al, above n 28, 22. The Domino's Pizza network provides a more concrete example of the division between company-owned units and franchised units. In 2013, the FWO noted that approximately 80% of Domino's stores were operated by franchisees whilst the remaining stores are owned and operated by Domino's Pizza Enterprises Limited. See Fair Work Ombudsman, 'Final Report on the Proactive Compliance Deed between Domino's Pizza Enterprises Ltd and the Fair Work Ombudsman' (July 2013) 4.

<sup>40</sup> 7-Eleven Inquiry, above n 23, 67.

<sup>41</sup> *FW Act*, s 550.

<sup>42</sup> *FW Act*, s 45. See, eg, *Fair Work Ombudsman v Devine Marine* [2015] FCA 370; and *Potter v Fair Work Ombudsman* [2014] FCA 187; *Fair Work Ombudsman v Mhoney Pty Ltd & Anor* [2016] FCCA 2959.

<sup>43</sup> *Keller v LED Technologies Pty Ltd* [2010] FCAFC 55.

<sup>44</sup> *Giorgianni v The Queen* (1985) 156 CLR 473; *Young Investments Group Pty Ltd v Mann* (2012) 293 ALR 537, 541.

were unwilling to provide evidence to the FWO about their own conduct or the conduct of others.<sup>45</sup> The lack of relevant evidence meant that the FWO believed that it was not in a position to prove that 7-Eleven Stores had been ‘knowingly concerned’ in the contraventions of its franchisees and therefore unable to institute proceedings against 7-Eleven Stores on this basis. The proposed reforms in Schedule 1, Part 4 may allow the FWO to better address these evidentiary issues, albeit these additional investigatory powers are not without some drawbacks.<sup>46</sup> An alternative way in which to address some of the evidentiary problems facing the FWO – particularly where employment records are absent or inaccurate – is to shift the onus of proof to the alleged wrongdoer.<sup>47</sup>

Addressing the evidentiary issues does not, however, resolve the more fundamental regulatory challenge raised by the accessorial liability provisions. In particular, if liability pivots on whether a lead firm (e.g. a franchisor) was ‘knowingly concerned’ in a contravention committed by another (e.g. an employer entity), the regulatory framework may not properly address the risk of ‘counterproductive liability avoidance’.<sup>48</sup> This is where firms seek to rework their contractual relationships to avoid being held liable for employment contraventions. This may involve reducing (rather than expanding) the extent to which they monitor and direct their franchisees’ compliance practices and may contribute to, rather than curtail, worker exploitation in this context. Previous research into third party liability regimes suggests that any regulatory extension must be framed in such a way to avoid the problem identified by the FCA - that is, legislative amendments ‘will see a diversion of effort towards avoidance, rather than compliance’.<sup>49</sup> To a large extent, we believe that the duty-based standards imposed under s 558A-558B are designed in such a way to avoid these issues.

Second, as discussed above, it has been argued that the laws may be detrimental to the economy in so far as they threaten the viability of the franchise model. While it is true that the allocation of risk within the franchise arrangement may be recalibrated by the proposed reforms, it is doubtful whether the consequences will be nearly as dire as predicted. The FCA has argued that requiring franchisors to monitor and audit their franchisees’ workplace practices would be ‘highly likely to undermine the fundamental purpose of the franchise model.’<sup>50</sup> However, this seems to overlook the fact that many franchisors are already engaged in close monitoring of their franchisees in relation to product and service quality.<sup>51</sup> It also

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<sup>45</sup> Ibid 72.

<sup>46</sup> See discussion below.

<sup>47</sup> For further discussion of this proposal, see Hardy 2016, above n 11.

<sup>48</sup> Cynthia Estlund, ‘Who Mops the Floor at the Fortune 500? Corporate Self-Regulation and the Low Wage Workplace’ (2008) 12(3) *Lewis & Clark Law Review* 671, 692.

<sup>49</sup> Franchise Council of Australia, ‘Supplementary Submission to the Minister’ (20 February 2017) (‘FCA Supplementary Submission’) 4.

<sup>50</sup> Ibid.

<sup>51</sup> Ashlea Kellner, David Peetz, Keith Townsend and Adrian Wilkinson, “‘We are very focused on the muffins’”: Regulation of and compliance with industrial relations in franchises’ (2016) 58 *Journal of Industrial Relations* 25.

appears to underplay a range of other important advantages of franchising over other organisational forms. In particular, franchising offers franchisors ‘to grow their business by allowing others to use the model they have developed, within an agreement that allows them to retain substantial control over its use but without the financial risks of significant capital expenditure.’<sup>52</sup>

As noted above, instead of making franchisors legally liable for the workplace misdemeanours of their franchisees, there has been a push to leverage brand and reputational concerns of franchisors in a bid to enhance employer compliance. While there is an important place for voluntary governance mechanisms, there is also growing evidence that these ‘softer’ tools may not be sufficient in prompting and sustaining franchisor commitment to workplace compliance and effectively tackling systemic underpayment within franchise networks (especially in the absence of any threat of legal sanctions).<sup>53</sup> For example, the FWO’s inquiry into 7-Eleven found that the franchisor ‘had a reasonable basis on which to inquire and act’<sup>54</sup> into allegations of franchisee non-compliance with employment standards over a five year period, and yet 7-Eleven head office largely failed to take any substantive steps to curb employer non-compliance in this time (at least prior to the public airing of these issues). The fundamental weakness of voluntary initiatives is further underlined by the fact that 7-Eleven head office was specifically invited to participate in the FWO’s national franchise program – which was designed to leverage the franchise relationship in a way that enhanced employment standards compliance amongst franchisees – but expressly declined to do so.<sup>55</sup>

Following the fallout from the 7-Eleven scandal, the then General Manager of the FCA, Mr de Britt, met with senior executives of the FWO to discuss how the FCA could work more closely with the FWO and ensure that all franchises were not being unfairly ‘tarded with the same brush’.<sup>56</sup> At the time of the meeting in late 2015, Mr de Britt apparently expressed confidence that:

FCA members are more than keen to work with the FWO to ensure and promote compliance with workplace laws and give the broader community greater confidence that their commitment to compliance is both sincere and real.<sup>57</sup>

Yet, when the FWO wrote to eight CEOs of franchisor entities inviting them to enter into a ‘compliance partnership’ with the FWO – only one franchise network ultimately decided to

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<sup>52</sup> Parliamentary Joint Committee on Corporations and Financial Services, *Opportunity Not Opportunism: Improving Conduct in Australian Franchising* (Commonwealth of Australia, December 2008) 5.

<sup>53</sup> Tess Hardy, ‘Brandishing the Brand: Enhancing Employer Compliance through the Regulatory Enrolment of Franchisors’ (Paper presented at the Labour Law Research Network Conference, Amsterdam, 25-27 June 2015).

<sup>54</sup> *7-Eleven Inquiry*, above n 23, 67.

<sup>55</sup> For further discussion of the National Franchise Program, see Hardy 2015, above n 53.

<sup>56</sup> James 2016, above n 27, 4.

<sup>57</sup> *Ibid.*

engage with the regulator on a serious basis. The remaining seven franchisors either declined or ignored the invitation.<sup>58</sup> Again, this example highlights some of the problems with seeking to rely solely on voluntary or self-regulatory initiatives in the absence of direct incentives or threats to compel or coerce involvement of lead firms in compliance initiatives.

In any event, there is now evidence to suggest that voluntary compliance partnerships may not be as effective in addressing deliberate non-compliance as initially thought. In particular, Domino's Pizza has previously entered into two compliance deeds with the FWO. Under these deeds, the franchisor agreed to undertake a self-audit for delivery drivers and in-store employees, amongst other things.<sup>59</sup> Notwithstanding the franchisor's long-term cooperative relationship with the FWO, and its public commitment to promoting and ensuring workplace compliance amongst its franchisees, serious concerns have now been raised about working conditions and employer compliance across the Domino's network.<sup>60</sup>

The final point we wish to address before considering the proposed provisions is the FCA's complaint that the franchising sector is being 'singled out when many egregious workplace law breaches have occurred in non-franchised structures'.<sup>61</sup> We would tend to agree that there are good reasons, and strong evidence, for capturing other types of fragmented organisational structures and business networks, including complex supply chains and labour hire arrangements.<sup>62</sup> The failure to extend liability to these other lead firms represents a significant gap.

### *Recommendation Two*

In addition to franchise networks and corporate groups, other types of organisational forms (including supply chains and labour hire arrangements) should be captured by Division 4A.

### *Specific Comments on Schedule 1, Part 2*

#### *Section 558A*

One of the most challenging aspects of this reform is how to confine the potential franchisor defendants in order to ensure that any proposed liability scheme not only remains workable

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<sup>58</sup> Ibid 4.

<sup>59</sup> Proactive Compliance Deed between the Commonwealth of Australia (as represented by the Office of the Fair Work Ombudsman) and Domino's Pizza Enterprises Limited (19 December 2011).

<sup>60</sup> See, eg, Toscano, above n 21.

<sup>61</sup> FCA Supplementary Submission, above n 49, 4.

<sup>62</sup> For further discussion of these other types of lead firms, see Hardy 2016, above n 11.

in practice, but is best placed to achieve the normative objectives set out in the Explanatory Memorandum. These aims include:

- a) to prevent and deter franchisors and holding companies from operating on ‘a business model based on underpaying workers’;<sup>63</sup> and
- b) to prompt these lead firms to do more ‘to protect vulnerable workers employed in their business networks.’<sup>64</sup>

Unlike the accessorial liability provisions, which apply to all ‘persons’ who are found to be ‘involved in’ the relevant contraventions, the scope and application of proposed s 558A pivots on the definition of ‘responsible franchisor entity’ and ‘franchisee entity’. While the Explanatory Memorandum suggests that the definition of ‘responsible franchisor entity’ is generally consistent with the approach taken under the Franchising Code of Conduct,<sup>65</sup> it appears that this is not strictly the case.

Clause 5 of the Franchising Code sets out a very detailed definition of ‘franchise agreement’ and separately and respectively defines ‘franchise system’, ‘franchise’,<sup>66</sup> ‘franchisor’,<sup>67</sup> ‘franchisee’, ‘master franchise’, ‘subfranchisor’, ‘associate’ and ‘interest in a franchise’ in clause 4. In our view, the definitions of key terms used in the Franchising Code provide greater clarity and certainty than the proposed definitions of ‘franchisee entity’ and ‘responsible franchisor entity’ in s 558A(1)-(2). In particular, the Franchising Code expressly contemplates and provides for a range of multi-level franchises, as well as franchises which operate through complex corporate groups.

The other critical limit placed on the scope and application of these provisions is that in order for a person to be characterised as a ‘responsible franchisor entity’, it must be proved that the person ‘has a significant degree of influence or control over the franchisee entity’s affairs’.<sup>68</sup> The Explanatory Memorandum makes clear that the term ‘affairs’ is not defined but is intended to be read broadly, and is not limited to particular aspects of a franchisee’s

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<sup>63</sup> Explanatory Memorandum, Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017 (Cth) (‘Explanatory Memorandum’) 6.

<sup>64</sup> Ibid.

<sup>65</sup> The Franchising Code of Conduct is set out in Schedule 1 of the *Competition and Consumer (Industry Codes – Franchising) Regulation 2014* (Cth).

<sup>66</sup> Section 4 of the Franchising Code defines ‘franchise’ to include the following: a) the rights and obligations under a franchise agreement; b) a master franchise; c) a subfranchise; and d) an interest in a franchise.

<sup>67</sup> ‘Franchisor’ is defined as included the following: a) a person who grants a franchise; b) a person who otherwise participates in a franchise as a franchisor; c) a subfranchisor in its relationship with a subfranchisee; d) a subfranchisor in a master franchise system; e) a subfranchisor in its relationship with a franchisee.

<sup>68</sup> Vulnerable Workers Bill, s 558A(2)(b).

operations. Rather, it is intended to include involvement in the franchisee's financial, operational and corporate affairs.<sup>69</sup>

This wide definition of control is critical in addressing some of the legal and economic tensions which lie at the heart of franchising relationships. On the one hand, a defining feature of a typical franchising arrangement is the franchisee's legal independence from the franchisor: this contractual disconnect means that the franchisee operates the business at its own peril and generally assumes the commercial risks of doing so. While franchisees may be legally independent from the franchisor, they are economically dependent on these lead firms with franchisors exercising a high degree of control over franchisees' management and trading practices.<sup>70</sup> Indeed, while franchisors frequently claim that they have no influence over the wages that franchisees pay to workers, others have argued that franchisors effectively control wages 'by controlling every other variable in the business except wages'.<sup>71</sup>

### *Section 558B*

Section 558B(1) represents an important extension of the current laws, and addresses some of the shortcomings of the accessory liability provisions. In particular, as noted above, s 550 of the FW Act is problematic because of the need to prove that the person had *actual knowledge* of the essential elements of the contravention. In comparison, s 558B(1) allows the court to take into account not only what the responsible franchisor entity (or one of its officers) 'knew' about the contravention of the franchisee entity, but what it (or the officer) 'could reasonably be expected to have known'. In short, the provisions capture not just actual knowledge, but constructive knowledge. The Explanatory Memorandum makes clear that knowledge will be assessed on an objective basis taking into consideration relevant circumstances, including the responsible franchisor entity's knowledge, experience and acumen. By expanding the knowledge requirement in the way proposed, s 558B(1) potentially overcomes one of the most challenging aspects of the accessory liability provisions as they presently apply to fragmented work arrangements, such as franchise networks.<sup>72</sup> Further, in directing the court to apply a standard of reasonableness – in this subsection and others – the provisions avoid some of the problems generally associated with strict liability provisions.<sup>73</sup>

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<sup>69</sup> Explanatory Memorandum, above n 63, 8.

<sup>70</sup> See, eg, Weil 2014, above n 15; Richard Johnstone, Shae McCrystal, Igor Nossar, Michael Quinlan, Michael Rawling and Joellen Riley, *Beyond Employment: The Legal Regulation of Work Relationships* (Federation Press, 2012).

<sup>71</sup> Catherine Ruckelshaus et al, *Who's the Boss: Restoring Accountability for Labor Standards in Outsourced Work* (National Employment Law Project, Report, 2014) 11.

<sup>72</sup> Hardy 2016, above n 11, 105.

<sup>73</sup> *Ibid* 106.

The responsibilities placed on franchisors (and holding companies for that matter) is confined in a number of important ways.

First, responsible franchisor entities can only be held liable under s 558B(1) for certain prescribed contraventions of the FW Act by their franchisee entities. The relevant civil remedy provisions include contraventions of modern awards and enterprise agreements and breaches of record-keeping obligations and sham contracting provisions, amongst others. Notably absent is reference to the civil remedy provisions of the FW Act which deal with adverse action. In our view, the relevant provisions which have been prescribed under s 558B(7) strike the right regulatory balance. We note that the FCA has raised concerns about the inclusion of the sham contracting provisions, amongst others. However, in light of various examples of franchisees engaging in sham contracting in a deliberate and routine manner,<sup>74</sup> it is essential that s 558B(7) includes the sham contracting provisions so as to ensure that the franchisor takes an active interest in (and does not turn a blind eye to) dubious contracting arrangements which are designed to circumvent workplace protections.

The second critical way in which these provisions are circumscribed is via the statutory defence set out in s 558B(3). This subsection provides that the person (i.e. a franchisor, a holding company or a relevant officer) will not contravene s 558B(1) or 558B(2) if, at the time the contravention took place, the 'person had taken reasonable steps to prevent a contravention by the franchisee entity or subsidiary of the same of similar character.'<sup>75</sup> In determining whether a person took such 'reasonable steps', the court is directed to have regard to a range of relevant matters, including: the size and resources of the franchise; the extent to which the person had the ability to influence or control the contravening employer's conduct; and any action the person took to inform the employer of the relevant workplace laws and obligations and any arrangements the person had in place for assessing the employer's ensuing compliance with workplace obligations.

This is a non-exhaustive list and therefore the court may take into account any other matter it considers relevant in determining whether the person has taken reasonable steps to prevent the contravention.

By placing broad, positive duties on the franchisor, holding companies and officers, s 558B(3) effectively allows the court to undertake a fact-sensitive analysis which takes into account the full range of circumstances. Imposing reasonable standards of diligence can be more administratively burdensome and less certain than strict liability regimes, however, the great advantage is that courts are provided with sufficient flexibility to adjust the

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<sup>74</sup> Adele Ferguson and Sarah Danckert, 'Wage fraud: Pizza Hut franchisees using 'sham' contracts to underpay drivers', *The Sydney Morning Herald*, 23 November 2015; Peter Ryan, 'Pizza Hut Fair Work audit finds delivery drivers underpaid, franchisees breaching workplace laws', *ABC News*, 27 January 2017.

<sup>75</sup> Vulnerable Workers Bill, s 558B(3).

liability standard so as to reflect the diversity of franchising arrangements (and corporate structures). This provision is specifically designed to minimise concerns that courts will ‘set standards or make assumptions based on the resources of larger [franchise] systems.’<sup>76</sup> It is also designed to promote the right type of liability avoidance on the part of lead firms – that is, by encouraging franchisors and holding companies to do more (not less) in terms of enhancing compliance with workplace laws across their respective business networks.

### *Section 558C*

This section – which allows the franchisor or holding company who has rectified an underpayment to recover those monies from the franchisee or subsidiary who committed the primary contravention – is an important way in which to guard against opportunism on the part of the direct employer. In particular, it has been observed that holding third parties accountable for employment contraventions and absolving the liability of the direct employer ‘may create a moral hazard, as primary wrongdoers face decreased incentives to manage risks or comply with the law, knowing that they will not bear the costs.’<sup>77</sup> This provision addresses these issues.

### *Recommendation Three*

To reduce confusion and enhance clarity, the terms ‘franchisee entity’ and ‘responsible franchisor entity’ in s 558A should be defined to more closely reflect the definitions of similar terms (such as ‘franchise’, ‘franchisor’ and ‘franchisee’) in the Franchising Code of Conduct.

### ***Schedule 1, Part 3 – Unreasonable requirements to make payments***

We welcome the intent of these amendments. They aim to deal with ‘cash-back’ practices identified in the Fair Work Ombudsman’s report into 7-Eleven and the possibility of section 326 of the *Fair Work Act* not prohibiting such practices.<sup>78</sup> This risk of the latter arises from the possibility that two elements of section 326 are narrowly construed: 1) ‘requirement’ is interpreted as being restricted to legal obligation hence, not extending to unlawful conduct as was evident in the case of 7-Eleven; 2) ‘spend’ requires expenditure on goods and services and does not extend to bare payments of cash to employers.

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<sup>76</sup> FCA Supplementary Submission, above n 49, 5.

<sup>77</sup> Rogers, above n 22, 38, citing R Kraakman, ‘Third Party Liability’ in Peter Newman (ed) *The New Palgrave Dictionary of Law and Economics* (Macmillan Reference, 1998).

<sup>78</sup> 7-Eleven Inquiry, above n 23, 59-60.

While the intent of these amendments is commendable, the amendments as presently drafted fall short in four respects. There is, firstly, no clarification that ‘requirement’ can extend to unlawful conduct.

Second, there is inadequate clarity as to the meaning of ‘unreasonable’. Specifically, the Explanatory Memorandum to the Bill provides that:

89. Asking an employee for ‘cashback’ so the person can keep their job, or with the sole purpose of undercutting their minimum entitlements under the Fair Work Act, will always be unreasonable and prohibited under section 325(1).

90. Asking an employee for any amount to be spent, or money to be paid, out of the employee’s pocket in a way which involves undue influence, duress or coercion, will always be unreasonable and prohibited under section 325(1).

The clarification as to the meaning of ‘unreasonable’ provided in the Explanatory Memorandum has not, however, been incorporated into the amendments – and should be.

Third, under the amendments, ‘unreasonable’ payments will only be in breach of section 325 if ‘the payment is directly or indirectly for the benefit of the employer or a party related to the employer’. Whilst in practice, this additional requirement of benefit might not matter in most situations, it is wrong in principle – it allows for lawful ‘unreasonable’ payments that do not meet this requirement of benefit. This requirement should be removed.

Fourth, the scope of the amendments should be extended to prospective employers and employees. This is to deal with the practice of prospective employers extracting payments from 417 visa-holders in return for jobs that will allow these workers to gain a second year work rights visa.<sup>79</sup>

#### *Recommendation Four*

Amendments to section 325 of the *Fair work Act* should be changed to:

- Clarify that a ‘requirement’ can be imposed through unlawful conduct;
- Elaborate on the meaning of ‘unreasonable’ as provided under the Explanatory Memorandum to the Bill;

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<sup>79</sup> Fair Work Ombudsman, *Inquiry into the Wages and Conditions of People Working under the 417 Working Holiday Visa Program* (2016) 3-4.

- Remove the requirement of benefit for the employer or a party-related to the employer in relation to ‘unreasonable’ payments; and
- Extend to prospective employers and employees.

#### *Schedule 1, Part 4 – Powers of the FWO*

Whilst we appreciate of stronger powers being conferred upon the Fair Work Ombudsman in relation to employers suspected of breaching the *Fair Work Act*, we are concerned that the extension of these powers to *workers* may undermine their legal rights by further inhibiting the provision of information by workers to the Ombudsman.

Workers may not voluntarily provide information to the Ombudsman for fear they may be subject to the coercive powers proposed by these amendments. This is a particular acute risk for temporary migrant workers who have worked in breach of their visas (or perceive themselves to be in such breach). This risk was evident in relation to 7-Eleven where the Ombudsman noted that:

Student visa holders working in 7-Eleven stores confirmed a reluctance to report underpayments or cooperate with FWO investigations for fear of being investigated by another government regulator. Some appeared to be breaching visa conditions and not paying correct tax which adds to their reluctance.<sup>80</sup>

If exercised against workers whose legal rights under the *Fair Work Act* have not been respected, these powers can result in the provision of information on breaches by the workers of other laws, notably immigration laws; such information could then be used as the basis of cancelling the visas of these workers. In other words, these coercive powers could result in the provision of information by exploited workers that results in their deportation. This risk, we fear, will worsen the ‘culture of complicity’ that results in the exploitation of temporary migrant workers (as was found by the Ombudsman in relation to 7-Eleven).<sup>81</sup>

It should be noted here that the provision of the Bill that provides for protection from liability relating to these powers do not prevent such a result (proposed section 712D of the *Fair Work Act*) as they only provide protection in relation to the giving of information, production of record or document and answering of questions. They do not provide protection from liability in relation to the conduct that is disclosed through the giving of information etc.

The provisions relating to use/derivative use indemnity (proposed sections 713(2)-(3) of the *Fair Work Act*) are also unlikely to prevent situations where the provision of information by

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<sup>80</sup> 7-Eleven Inquiry, above n 23, 59-47.

<sup>81</sup> Ibid 32.

exploited workers through the exercise of these coercive powers results in their deportation. This is because these provisions apply only to ‘proceedings’, usually understood as court or tribunal processes. As such, they will probably not apply to exercise of administrative powers such as the power of the Immigration Minister to cancel visas.<sup>82</sup>

For all these reasons, we recommend that these powers can only be exercised in relation to workers whose rights under the *Fair Work Act* are suspected to have been breached when there are compelling reasons.

#### *Recommendation Five*

Part 4, Schedule 1 of the Bill be amended so that the powers it proposes can only be exercised in relation to workers whose rights under the *Fair Work Act* are suspected to have been breached when there are compelling reasons.

#### *Vital migration law reforms*

A major shortcoming of the Bill is that it fails to provide for crucial reforms of immigration laws that will reduce the vulnerability of temporary migrant workers. As the Senate report, *A National Disgrace: The Exploitation of Temporary Migrant Workers*, recognised, there are ‘structural factors that create the vulnerability of temporary visa workers and predispose them to exploitation’.<sup>83</sup> This includes, as the report acknowledges, ‘the draconian consequences under the Migration Act that flowed from a temporary visa worker breaching a condition of their visa’.<sup>84</sup> It was this appreciation that led the Committee to make Recommendation 24:

The committee recommends that Section 116 of the *Migration Act 1954* be reviewed with a view to amendment such that visa cancellation based on noncompliance with a visa condition amounts to serious noncompliance. The committee further recommends that Section 235 of the *Migration Act 1954* be reviewed with a view to amendment such that a contravention of a visa condition amounts to a serious contravention before a non-citizen commits an offence against the section.<sup>85</sup>

Adoption of this recommendation will go a long way to reducing the vulnerability of temporary migrant workers who breach their visa in the performance work. Another option is the proposal made by Redfern Legal Centre for a new Ministerial Direction under s499 of the *Migration Act 1958* (Cth). This proposal is attached to the submission.

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<sup>82</sup> *Migration Act 1958* (Cth) s 116.

<sup>83</sup> Senate Inquiry – A National Disgrace, above n 1, 219; see also 143.

<sup>84</sup> *Ibid* 211.

<sup>85</sup> *Ibid* 261.

*Recommendation Six*

- Recommendation 24 of the Senate report, *A National Disgrace: The Exploitation of Temporary Migrant Workers* (2016) should be adopted; or
- The proposal for a new ministerial direction made by Redfern Legal Centre should be adopted.

Another source of vulnerability for temporary migrant workers who breach, or suspect they have breached, their visa conditions concerns the provision of information by the Fair Work Ombudsman to the Department of Immigration and Border Protection (pursuant to section 718 of the *Fair Work Act*). The possibility of such provision was clearly a factor behind the reluctance of 7-Eleven workers coming forward.<sup>86</sup>

It is recognized here that there needs to be a ‘firewall’ preventing the provision of such information in order to protect labour rights of migrants. Notably, the UN Special Rapporteur on the human rights of migrants has recommended in his end-of-mission statement that ‘the government implement “firewalls” between public services and immigration enforcement, thus offering better access to effective labour inspection’.<sup>87</sup>

*Recommendation Seven*

A ‘firewall’ should be enacted between the Fair Work Ombudsman and the Department of Immigration and Border Protection that prevents the provision of information by the Ombudsman to the Department in relation to workers who have contacted the Ombudsman.

We hope this submission has been of assistance.

Yours sincerely,

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<sup>86</sup> 7-Eleven Inquiry, above n 23, 58-59.

<sup>87</sup> UN Special Rapporteur on Human Rights of Migrants, *End of Mission Statement: Australia* (November 2016) 9 (available at <http://un.org.au/files/2016/11/16.11-SRM-Australia-End-of-mission-Statement.pdf>)