

## Turning 'quasi employees' into business managers

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## **Abstract**

Changes in the employment relationship in industrialized countries have resulted in many workers falling into a position of 'quasi self-employment'. In this situation, these workers must manage the business of selling their skills and time. This study, conducted in Queensland in 2004, reports some findings from a survey of workers in the building industry where many are engaged in short-term contract work that leaves their employment status ambiguous. With recent government intervention, they are being required to adopt more professional management. This paper explores their business attitudes and practices, particularly in relation to accounting and financial management systems, and the differences between those who regard themselves as employed and self-employed.

Keywords: SMEs, small business, building industry, accounting, business planning, quasi-employees, quasi self-employment

## **Introduction**

Since the 1970s, there has been a weakening in the employment relationship in industrialised countries as employers attempt to build greater flexibility into their employment systems (Campbell and Brosnan, 1999). Employment within organisations is now more likely to be for a fixed term, or part-time, or at less than standard hours. Also a smaller proportion of the work is done by workers internal to the organisation. Instead work previously done by internal workers is often now outsourced, or is franchised to previous employees, or is contracted to a self-employed workforce or to workers who are employed by a different company eg temporary employment agencies.

The result of these changes in employment has been an increase in the number of workers who do not have the full protection or benefits of employees, and contract their labour. The

distinction between contractor and employee can be difficult to define (Carby-Hall, 2002): in the US, for example, the Internal Revenue Service found it necessary to formulate a 20 question test to determine their status for tax purposes. Reflecting the more diverse nature of the employment system, the literature now refers not just to employees, self-employed and contractors, but also to 'quasi-employees', 'employment under another name', 'quasi- self-employment', 'quasi businesses', 'controlled self-employment', and 'the atypical workforce' (Star, 1986; Stanworth and Stanworth, 1995, Carby-Hall, 2002; Campbell and Brosnan, 1999). Regardless of the terms now used to describe the workers who find themselves in the self-employment grey area, these workers often have to comply with various types of legislation, and the 'business' that contracts their labour needs to succeed to keep these individuals gainfully working. Many of these workers need to become effective small business managers.

Small to medium enterprises (SMEs) around the world often come under the microscope not only because they are such important contributors to economic development, but also because of their high failure rates, often resulting from poor management practices. This paper examines the building industry in Queensland which is attempting to overcome some of the problems associated with poor business management by an education program aimed at workers who are self-employed, employees or working on contracts that possibly place them somewhere between contractors and internal workers.

### **The Building Industry**

The construction industry has the second highest proportion of self-employment of workers in Australia; only the agriculture, forestry and fishing industry is higher (ABS, 2004). However, in this industry, the distinction between employee and contractor is difficult to define.

“Many of those working in the construction industry who are called ‘self-employed’ are employees in all but name. Some of them have worked continuously for the same firm over several years and are in effect ‘in-house’ self-employed. Others have less regular and more casual work. In both cases they are quasi-employees, with little of the autonomy in the workplace which characterises those who are genuinely self-employed.” (Drucker, 1996:2 quoted in Brodie and Stanworth (2002))

Recent changes in legislation on workcover have resulted in attempts to define the relationship between employee and employer by setting conditions under which labour-only contractors may be regarded as employees. Failure to comply with this legislation has already resulted in thousands of dollars in backpay claims by employees (Cameron, 2004). It is becoming increasingly important therefore for builders to know their employment status and to manage their business and/or employment contract accordingly.

The building industry has been subject to criticism over the failure of many businesses in the industry and the subsequent costs to employees, sub-contractors, customers, and their suppliers. The industry has tried to tackle problems relating to poor business management through improved education and training. The Queensland Building Services Authority (QBSA) has recognised that small business operators and contractors in the building sector need more than good trades’ skills. As small business operators, building trades’ people need to acquire and develop business skills to prepare them to assume their responsibilities in the building industry. In recognition of the lack of distinction between employees and the self-employed, the QBSA requires all operators, not just those who currently own businesses, to

complete a management training course. They have approved Queensland Master Builders' Association (QMBA) to present financial management to all SMEs through intensive workshops. All operators who work on building sites must attend a three day workshop which includes two days on financial management practices. This is a major step in encouraging trades people to improve their business practices, as it extends the requirements from technical qualifications and experience into the management of a business. As part of a research project into the effectiveness of this program, this study explores the business practices and attitudes to business management of the workshop attendees, comparing those who consider themselves self-employed with those who regard themselves as employees.

### **Business management and failure in small business**

Numerous studies have been conducted on the causes of failure in small business (Berryman, 1983). External factors have been associated with between 35% and 50% of failures of small business (Everett and John, 1998), indicating that internal factors cause the majority of failures. Beaver and Jennings (2001, as cited in Davies, Hides et al. 2002) list as causes of failure: inadequate accounting systems, poor location, lack of marketing skills, lack of capital budget, inadequate provision for contingencies, lack of management skills, incompetence, lack of experience, neglect, fraud, disaster, poor record keeping, reckless money management, lack of formal planning, indifferent employees, inability to cope with growth and excessive inventory. As this extensive list of factors leading to small business failure indicates, many of the factors identified as causes of failure are internal to the firm, and associated with the lack of skills and competencies of management. The main problems can be attributed to poor management, in particular the inability to plan for the future, inadequate record keeping and the poor use of information to control business activities. This research focuses on record

keeping, accounting systems, formal planning and the collection and use of financial information by SMEs.

### **Incorporation, employees and business managers**

It is becoming increasingly difficult to define who is a small business owner. Many people who work as employees in the sense that they provide their labour exclusively to a business for an extended period of time, now do so by contracting through their own company or as sole traders. They are employed by the company and also own and manage their own business (often with another family member) which contracts out their labour. This practice is particularly common in the building industry and workplace insurance is influenced by legal status. In this research, respondents were asked whether they are employed or self-employed so their categorisation is by self-definition, not by legal definition.

Tradespeople who form a company or business entity to contract out their services may have an advantage in areas such as risk management, tax and contractual status but there are onerous requirements to managing a company. The difficulties and additional costs faced by small businesses who decide to incorporate have recently been highlighted by changes to the taxation laws in the UK which have encouraged small firms to incorporate (Rae, 2004).

There are advantages and disadvantages to all legal structures, and for the entrepreneur with multiple business and personal goals, it can be difficult to choose the most appropriate structure (Khandekar and Young, 1985). For building industry tradespeople there are obvious additional expenditures of both time and money to maintain a corporate structure. There may be taxation advantages to incorporation but many SMEs do not fully understand when there is value in incorporation to receive taxation advantages. However the pressure to incorporate may also come from other businesses who prefer to outsource work to a company rather than

have employees or sole traders which would require them to comply with employment legislation. In this exploratory research, participants are asked to nominate their legal status and to indicate if they are under pressure to incorporate.

### **Maintaining records and understanding accounting systems**

Many builders and others involved in the building and construction industry work long hours (often 6am to 6pm actually on the site), so they have little time to invest in accounting-type tasks. Accounting tasks are generally given low priority, but the literature indicates that owners should take a proactive approach and make time for regular book keeping which would keep them informed of their bottom line and help them to make better decisions that would lead to success and growth (Campbell, 2001). Financial problems in SMEs have been linked by Day and Taylor (2002) to the poor quality of accounting information. Accounting literature tells us that financial information needs to have the characteristics of relevance, quality, and timeliness to make it useful for decision making. This accounting information is required for internal control in the business as well as for external reporting (for example, to banks) (Atrill, McLaney, Harvey & Jenner, 2003). Day and Taylor (2002) concluded that many owner-managers did not have any formal or informal training in basic accounting and business skills and this often led to financial problems and eventually, financial distress.

Research conducted in the UK in 1999 by Collis and Jarvis (2002) demonstrates that financial management is crucial to the survival and success of small enterprises. Their study concluded that small businesses rely on the bank and the external accountant as sources of financial information and this information may be neither timely nor relevant. While accountants and banks provide information on liquidity and profitability, they can not be expected to provide

information on costs or operating expenses and contingences that businesses need to understand and control.

Cleland (2001) suggested that small businesses need to have management accountants involved in the day to day decisions, such as pricing, to help turn around deteriorating financial performance and to effectively price a product, or, in the case of builders, service business managers and operators need to understand their true costs' structure. A UK study by Reid and Smith (2002), argued that, although small firms are innovative and flexible, they have difficulty in structuring their pricing. Small firms were categorised by Reid and Smith (2002) as adaptive, running blind or stagnant. They found that only 20% were in the adaptive category, 40% were running blind and the other 40% were stagnant. They concluded that a management accounting system was vital to small businesses survival and coping with change. However it is questionable whether small businesses could in fact afford accountants on a day-to-day basis.

Many small businesses run into cashflow problems during both startup and shaky economic conditions. This is often because they fail to understand the importance of cashflow and do not set aside cash for contingences such as down time due to sickness or poor economic conditions. Rather, many SMEs in the building and construction industry take more cash out of the business and spend it in the good times and maintain little or no cash in reserve for the lean times. McCrea (2002) argues that SMEs should ensure that they do credit checks and tap into accounting and financial professionals for assistance to overcome these problems. Similarly, Wijewardena, De Zoysa, Fonseka, & Perera (2004) maintain that planning and control is important for business performance in SMEs. Operators need to understand how their business is performing and put in place controls to ensure they maintain profitability

throughout the business cycle rather than on a week by week basis. This requires the business to have plans with which to compare performance. Planning, however, is largely ignored and operators often argue that they cannot plan, as the future is too uncertain.

### **Strategic and operational planning and control**

Multiple studies have been conducted that attempt to relate planning to the performance of small businesses. Business plans, which change with the business, are purported to be a roadmap to success to keep competitors at bay and refocus strategy to meet the daily operational challenges (Grimm, 2003). Planning for small business has been described by the level of sophistication, ranging from unstructured and intuitive, to structured operational and finally structured strategic planning (Bracker and Pearson, 1986). The sophistication of the planning has been positively related to financial performance in a range of industries (Robinson 1982; Bracker and Pearson 1986; Bracker, Keats et al., 1988). Moreover, studies such as these have established the importance of involvement of the entrepreneurs rather than ‘outsiders’ (Bracker, Keats et al. 1988). In order to gain a better understanding of the importance that SMEs place on planning, participants in this study were asked to indicate their attitude to budgeting, costing and business planning.

### **Seeking advice**

While many business operators need to access advice and bounce ideas off other people, they often simply ask other business operators what they know rather than seeking expert advice. Many SMEs see professional advice as a cost rather than an investment and prefer to invest in plant and equipment rather than advice that has the potential to give them a far greater return. For most SMEs, their accountants are generally considered the major source of advice for the business (Kirby and King 1997; DEWRSB 1998; Leighton and Schaper 2003) The nature of

the accounting profession may be changing and there is a perception according to Kirby and King (1997) that accounting professionals are not necessarily considered the best source of broad-based management advice. Nonetheless many small operators and even larger businesses can get into major difficulties as they fail to maintain adequate records, understand their cost and pricing structures and manage financial risks associated with their business and in all these areas accountants can provide professional advice.

## **Methodology**

This exploratory study used a self-administered questionnaire to survey participants in an accounting workshop conducted by the Queensland Masters Builders' Association (QMBA) during 2004. A total of 81 builders and building trades' people participated in the workshops and 75 usable questionnaires were returned. The workshops were conducted across five weekends with five different groups of participants. Participants were involved in a diverse range of building activities including building and carpentry, plumbing, painting, concreting, bricklaying and glazing. This paper uses cross tabulation to examine some of the relationships between employed and self-employed business men and women and their methods of accounting and financial management. This paper also examines their perceptions of the importance of several good financial management practices.

## **Results**

Participants were asked how they operated their businesses or how the businesses in which they were employed were operated. As can be seen in Table 1 more than two-thirds of the participants operated as, or worked for sole traders or partnerships.

**Table 1: Participants by business type**

<b>Business Type</b>	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Sole trader	21	14	35
Partnership	15	2	17
Company	1	12	13
Trust	0	0	0
Franchise	0	2	2
No answer	0	8	8
<b>Total</b>	<b>37</b>	<b>38</b>	<b>75</b>

The age of respondents and their employment status was also analysed (Table 2). The data suggests that tradespeople are more likely to start businesses as they grow older. In fact there were very few employees in the over 45 year olds. Much construction work involves heavy labour and the small number of employees over 45 may result from a migration by aging employees to other less physically demanding industries.

**Table 2: Age of the participants**

<b>Age</b>	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Less than 25	3	11	14
25-34	15	17	32
35-44	10	7	17
45 or more	9	3	12
<b>Total</b>	<b>37</b>	<b>38</b>	<b>75</b>

There is little pressure on trades people to operate their business as a company as can be seen from Table 3, which shows that 62% of respondents are under no pressure to trade as a company. There is more pressure on some self-employed trades' people to have a company structure. This is surprising as it is easier for incorporated businesses or registered partnership to qualify as subcontractors rather than employees for WorkCover.

**Table 3: Are you under pressure to trade as company**

	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Yes	4	2	6
No	32	20	52
No answers	1	16	17
<b>Total</b>	<b>37</b>	<b>38</b>	<b>75</b>

Although no questions were asked concerning the marital status of respondents, many partner/spouses were actively involved in the management of the business. From the responses summarised in Table 4 almost 55% of respondents had a partner/spouse involved in the management of the business. What is notable is the number of spouses involved among the group who regarded themselves as employees.

**Table 4: Is your spouse involved in the management of your business**

	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Yes	21	11	32
No	15	12	27
No answer	1	15	16
	37	38	75

When asked who maintained the financial records of the business respondents in several cases gave more than one response and this is evident in Table 5 with a total of 93 responses. Most participants maintained some records themselves, but it is surprising that so few businesses (approximately 25%) reported that their accountant had a role in keeping financial records. The employed were almost as likely to use an accountant.

**Table 5: Who maintains your financial records?**

	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Self	23	15	38
Partner	13	10	23
Accountant	12	8	20
Other	1	4	5
No answer	1	6	7

Table 6 shows the financial records kept by employed and self-employed respondents. Respondents were able to provide more than one answer to the question regarding the types of financial records they keep. The most common record was weekly income, which indicates that most were working on a short time frame.

Out of the 37 self-employed, 31 provided information on the records they keep. Eighteen keep full financial records, nine keep partial records of operations (income and/or operating expenses) and four keep other mixes of records. Some of these self-employed believe that they are not reporting income via GST statements with only 23 of the 31 self-employed respondents using these statements. Of the 23 keeping GST statements almost all of these also maintained monthly income statements, details of operating costs, and before and after tax profit. There was no relationship between the range of records kept and the use of accountants to maintain accounting records.

For employees, the record most often kept was for weekly income. Further analysis of these answers provided the following information. Of the 38 who classed themselves as employees, 27 answered these questions. Of these 27, sixteen keep records of their income only and five appear to keep full business records. The remaining employees keep both income and expense records which is consistent with contractor/employee requirements.

**Table 6: Which of the following financial records do you currently keep?**

	<b>Self-employed</b>	<b>Employed</b>	<b>Total</b>
Annual turnover	14	8	22
Weekly income	22	22	44
Monthly income	22	6	28
Operating expenses	26	7	33
Before tax profit	16	6	22
After tax profit	19	7	26
GST statements	23	4	27
No answer	6	11	17

However, the way many businesses keep records may not have improved a great deal since the introduction of GST. In this survey, 12% of those surveyed still kept records in a shoe box, 7% in the glovebox of the car, and 34% in a filing cabinet. Only 16% kept a detailed cash book or journal and 9% keep a written summary.

Attendees were asked whether they agreed with a series of statements related to the management (mainly financial management) of their business. The results are summarised in Table 7.

**Table 7 The importance of financial management**

	Self-employed			Employed		
	Disagree	Neutral	Agree	Disagree	Neutral	Agree
Budgeting is essential to the everyday running of my business	2	6	27	0	2	31
Having a cost plus formula for calculating the price of jobs is essential	2	7	26	0	2	28
Owning plant, equipment and machinery is better than leasing	2	13	18	2	9	19
It is important that my business runs at a profit every week	4	5	24	2	5	24
It is important to set aside money for contingencies such as holidays or illness	0	4	31	0	1	28
Insurance is a waste of money	24	5	6	26	1	3
Understanding depreciation is important to my business	3	9	23	0	7	21
Understanding how to deal with bad debts is an important part of my business	2	4	29	0	1	31
A business plan is important to me	3	8	24	0	2	28
My accountant is an important source of business advice	3	6	26	0	2	28

The short term focus evident in Table 6 is reinforced in Table 7 where forty-eight respondents believed it was important to operate the business at a profit on a weekly basis. An area for some concern is the perception that it is better to own plant and equipment rather than leasing but it is probable that most respondents did not recognise that this ties up capital that could be used for other purposes. It is an issue that 35% of the self-employed did not know or disagreed with having a cost plus formula for pricing work. It is perhaps heartening that more than 83% of respondents regarded their accountant as an important source of business advice and do not see them as just a source of accounting expertise. However the most surprising finding was how little the self-employed and the employed differed in their attitudes.

## **Discussion and conclusion**

This survey focuses on an industry where it is difficult to classify the most skilled workers i.e. the tradespeople, as either employees or business owners. They may consider themselves as one or the other, but in fact the data seems to indicate that there is not a clear distinction. Those who considered themselves as employees were younger and less experienced than the self-employed, but they included several who apparently keep quite detailed records which suggest that they are, in fact, running a business. There was also a surprising level of involvement of their spouses in keeping records and managing their business for these people who considered themselves as employees. Nor did they differ substantially in their attitudes to management to those who consider themselves self-employed. Conversely some of those who consider themselves as self-employed act as though they are employees, some keeping no records apart from income. Moreover there was little difference in the attitudes to financial management of those who consider themselves self-employed and employees. This probably reflects the ambiguous employment status of many in this industry and their varied experiences as employees, contractors and employers.

The group of business operators and, in some cases, potential business operators responding to this questionnaire are in many cases failing to manage their business records, and particularly their financial records, in an appropriate way. Left to their current practices, many of the business people in this study are at higher risk of failure as they fail to keep adequate or appropriate records, have inadequate or no accounting systems, do not understand the need for formal planning - let alone have a plan - and they fail to collect and use information that is available to them. It is encouraging that accountants are seen as a source of business advice by almost all of the respondents and that most aspects of financial management are seen as important. However, the answers to questions about the financial

records currently kept by the business identify a gap between attitudes and practices.

Whether this is the result of a lack of time and/or resources for this activity, or because the industry is currently booming and financial management is not seen as very important in these conditions is unknown.

The financial management courses run by QMBA on behalf of QBSA are a worthwhile start to improving business practices. The courses are a one-off which introduce awareness; however, on-going reinforcement is required, plus efforts to encourage the attendees to actually implement good management practices. Few are currently maintaining even the most basic records necessary for a business, although they regard good management as important. The need for a plan for the business and management of risk may not become an issue for them until the next downturn in the industry. When that occurs, many who currently regard themselves as employees may be forced into self-employment.

The role of the accountant should be in giving business advice and encouraging small business owners to have good record keeping, rather than taking over small business' record keeping. There is more emphasis now on record keeping but this emphasis presently is on the records required for GST (goods and services tax) compliance. Professionals such as accountants need to reinforce requirements and practices that their clients need to implement to ensure business success. This role needs to be reinforced in the education and training given to accountants which should include more emphasis in the management areas. The majority of business clients that accountants deal with are SMEs, and, as professionals, should be providing more than tax and book keeping services to their clients. As accounting undergraduate degrees do not have room or leeway to introduce management courses,

accountants should be encouraged to study management and business courses in the post graduate mode or as part of their ongoing professional development and certification.

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