

## Comparing contractor rates with permanent salaries

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For many professionals, contracting is fast becoming a way of life; as such it is important employers understand how contractors work and what constitutes their hourly rate.

A good contractor should have a good knowledge of the industry they work in, the value of the services they're offering and a clear understanding of how employment costs are calculated.

### Factors to consider

Contractors and permanent employees differ in their rights and benefits. Permanent employees have access to a range of benefits which impact their actual available hours: annual leave, sick leave, paid public holidays, long-service leave, superannuation, jury leave, compassionate leave, family leave, professional development, access to bonus and incentive schemes and retrenchment/redundancy provisions. Employers need to be clear on whether they offer these benefits, because contractors will have to factor these into their hourly rate.

### How contractors work out their fee

Contractors work out their fee by calculating how many hours a year they'd work if they were a permanent employee, and then deducting hours to account for relevant benefits such as leave, superannuation, insurance and other benefits of regular employment. If the contract is short-term, they would also factor in potential downtime and overheads that may occur while they're searching for new work, say around 10-20%.

Based on a 40-hour week, the number of hours worked a year is 40 hours x 52 weeks = 2,080 hours a year. The table below covers benefits that need to be considered when converting a permanent salary into a contractor's hourly rate.

Benefits to consider	Breakdown of benefits per year	Total hours of benefits
Public holidays	11 days a year	88
Annual leave	20 days a year	160
Sick leave	5 days a year	80
Superannuation	5% of total hours a year	104
Professional indemnity	3% of total hours a year	62
Miscellaneous leave (e.g. family, jury duty)	3 days a year	24
Professional development	5 days a year	40
Total		558

#### Long-term Contracts:

To account for all of these factors in a contractor's hourly rate – this would be based on 2,080 hours per year - 558 hours of benefits = 1,522 hours.

#### Short-term Contracts:

To factor downtime into a short-term contract – let's say 15% - a contractor would divide the number of hours a year they're factoring into their rate by one, plus their downtime factor. So the rate would be based on 1,522 hours / (1 + 0.15) = 1,323 hours.

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### Example:

To work out a contractor's hourly rate, you would take the target salary and divide it by the total number of hours of benefits and work in a year.

For a target salary (before tax) of \$50,000 a year:

- For a full-time permanent employee, the hourly rate is  $\$50,000 / 2,080 \text{ hours} = \$24.04$ .
- For a long-term contract, the hourly rate is  $\$50,000 / 1,522 \text{ hours} = \$32.86$ .
- For a short-term contract, the hourly rate is  $\$50,000 / 1,323 \text{ hours} = \$37.79$ .

Based on all these factors, the hourly rate for a long-term contract is about 137% of a permanent employee's and 157% of a permanent employee's rate for a short-term contract.

Remember though, some contractors can charge a premium for their skills.<sup>2</sup>

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<sup>2</sup> Helen Sedcole, Senior HR Practitioner. (2009).