

# EMPLOYEE VS. INDEPENDENT CONTRACTOR

The IRS, Department of Labor, and the States are cracking down on classification between “Employee” and “Independent Contractor”. ***Maryland was one of four states who received a “performance bonus” from DOL as a reward for their success in detection of employee misclassifications during audits.***

Under common-law rules, anyone who performs services for you is your employee if you have the right to control what will be done and how it will be done. This is true even when you give the employee freedom of action. What matters is that you have the “right to control” the details of how the services are performed.

## **The IRS looks at three factors to determine how workers should be classified:**

1. **The behavioral test** focuses on whether the company controls or has the right to control what the worker does and how to do the job. If so, the worker is an employee. This includes instructions about performing the work, evaluation criteria and training. (Factors 1 thru 12)
2. **The financial test** looks at who controls the economics of the worker’s job. Factors favoring employee status include eligibility for reimbursement of travel costs and payment based on hours worked. Providing your own tools needed for the job is indicative of contractor status, as is being able to work for more than one firm. (Factors 13 thru 16)
3. **The type-of-relationship test.** Evidence of an employer-employee setup includes giving paid time off and retirement benefits, as well as hiring the worker to render services indefinitely rather than for a specific project. A written contract stating that the worker will be treated as an independent contractor isn’t determinative. (Factors 17 thru 20)

## **The 20 factors indicating whether an individual is an employee or independent contractor are:**

- 1) **Instructions:** An employee must comply with instructions about when, where, and how to work. Even if no instructions are given, the control factor is present if the employer has the right to control how the work results are achieved.
  - 2) **Training:** An employee may be trained to perform services in a particular manner. Independent contractors ordinarily use their own methods and receive no training from the purchasers of their services.
  - 3) **Integration:** An employee’s services are usually integrated into the business operations because the services are important to the success or continuation of the business. This shows that the employee is subject to direction and control.
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- 4) **Services rendered personally:** An employee renders services personally. This shows that the employer is interested in the methods as well as the results.
  - 5) **Hiring assistants:** An employee works for an employer who hires, supervises, and pays workers. An independent contractor can hire, supervise, and pay assistants under a contract that requires him or her to provide materials and labor and to be responsible only for the result.
  - 6) **Continuing relationship:** An employee generally has a continuing relationship with an employer. A continuing relationship may exist even if work is performed at recurring although irregular intervals.
  - 7) **Set hours of work:** An employee usually has set hours of work established by an employer. An independent contractor generally can set his or her own work hours.
  - 8) **Full-time required:** An employee may be required to work or be available full-time. This indicates control by the employer. An independent contractor can work when and for whom he or she chooses.
  - 9) **Work done on premises:** An employee usually works on the premises of an employer, or works on a route or at a location designated by the employer.
  - 10) **Order or sequence set:** An employee may be required to perform services in the order or sequence set by an employer. This shows that the employee is subject to direction and control.
  - 11) **Reports:** An employee may be required to submit reports to an employer. This shows that the employer maintains a degree of control.
  - 12) **Payments:** An employee is paid by the hour, week, or month. An independent contractor is usually paid by the job or on a straight commission.
  - 13) **Expenses:** An employee's business and travel expenses are generally paid by an employer. This shows that the employee is subject to regulation and control.
  - 14) **Tools and materials:** An employee is normally furnished significant tools, materials, & other equip by employer.
  - 15) **Investment:** An independent contractor has a significant investment in the facilities he or she uses in performing services for someone else.
  - 16) **Profit or loss:** An independent contractor can make a profit or suffer a loss.
  - 17) **Works for more than one person or firm:** An independent contractor is generally free to provide his or her services to two or more unrelated persons or firms at the same time.
  - 18) **Offers services to general public:** An independent contractor makes services available to the general public
  - 19) **Right to fire:** An employee can be hired by an employer. An independent contractor can not be fired so long as he or she produces a result that meets the specification of the contract.
  - 20) **Right to quit:** An employee can quit his or her job at any time without incurring liability. An independent contractor usually agrees to complete a specific job and is responsible for its satisfactory completion, or is legally obligated to make good for failure to complete it.
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