

# Employee or Independent Contractor

The IRS has very specific guidelines on if a person should be classified as an employee or independent contractor. An independent contractor is different from a standard employee. The business relationship between you and the individual will determine how the individual should be classified. A parish secretary is most likely always going to be an employee. The person cutting the parish lawn that you agreed on a price, a time frame (like once per week) and are not supplying any equipment will most likely always be an independent contractor. The Treasury Department estimates that employers nationwide misclassify millions of workers as independent contractors instead of employees, thus avoiding having to pay employment taxes. Misclassified employees often are denied access to critical benefits and protections they are entitled to by law, such as the minimum wage, overtime compensation, family and medical leave, and worker's compensation. Below is a list to help you determine if an individual should be classified as an employee or independent contractor.

## Internal Revenue Service Twenty Factor Test

### **Factor 1 No instructions**

Contractors are not required to follow, nor are they furnished with instructions to accomplish a job. They can be provided job specifications by the hiring firm.

### **Factor 2 No training**

Contractors typically do not receive training by the hiring firm. They use their own methods to accomplish the work.

### **Factor 3 Services don't have to be rendered personally**

Contractors are hired to provide a result and usually have the right to hire others to do the actual work.

### **Factor 4 Work not essential to the hiring firm**

A company's success or continuation should not depend on the service of outside contractor. An example violating this would be a law firm which called their lawyers independent contractors.

### **Factor 5 Set own work hours**

Contractors set their own work hours.

### **Factor 6 Not a continuing relationship**

Usually contractors don't have a continuing relationship with a hiring company. The relationship can be frequent, but it must be at irregular intervals, on call or whenever work is available. Warning: Part-time, seasonal or short-duration relationships have nothing to do with independent contractor status.

### **Factor 7 Control their own assistants**

Contractors shouldn't hire, supervise, or pay assistants at the direction of the hiring company. If assistants are hired, it should be at the contractor's sole discretion.

### **Factor 8 Time to pursue other work**

Contractors should have enough time available to pursue other gainful work.

### **Factor 9 Decide on job location**

Contractors control where they work. If they work on the premises of the hiring company, it is not under that company's direction or supervision.

**Factor 10 Order of work set**

Contractors determine the order and sequence they will perform their work.

**Factor 11 No interim reports**

Contractors are hired for the final result and therefore should not be asked for progress or interim reports.

**Factor 12 Paid by job**

Contractors are paid by the job, not by time. Payment by the job can include periodic payments based on a percentage of job completed. Payment can be based on the number of hours needed to do the job times a fixed hourly rate. However, this should be determined before the job begins.

**Factor 13 Work for multiple firms**

Contractors often work for more than one firm at a time.

**Factor 14 Pay business expenses**

Contractors generally are responsible for their incidental expenses.

**Factor 15 Have own tools**

Usually contractors furnish their own tools. Some hiring firms have leased equipment to their independent contractors-so they could show the contractor had their own tools and an investment in their business (see # 16). This strategy won't work if the lease is for a nominal amount or can be canceled by the hiring firm at will. In short, the lease must be equivalent to what an independent business person could have obtained in the open market. For more information, contact a labor attorney.

**Factor 16 Significant investment in their business**

Contractors should be able to perform their services without the hiring company's facilities (equipment, office furniture, machinery, etc.). The contractor's investment in his/her trade must be real, essential and adequate (see #15).

**Factor 17 Offer services to general public**

Contractors make their services available to the general public by one or more of the following:

- Having an office and assistants
- having business signs;
- having a business license;
- listing their services in a business directory;
- advertising their services.

**Factor 18 Can make entrepreneurial profit or loss**

Contractors should be able to make a profit or a loss. Employees can't suffer a loss. Five circumstances show that profit or loss is possible:

- If the contractor hires, directs and pays assistants;
- if the contractor has his/her own office, equipment, materials or facilities;
- if the contractor has continuing and reoccurring liabilities;
- if the contractor has agreed to perform specific jobs for prices agreed upon in advance;

- if the contractor's services affect his/her own business reputation.

### **Factor 19 Can't be fired at will**

Contractors can't be fired so long as they produce a result which meets the contract specifications.

### **Factor 20 No compensation for non-completion**

Contractors are responsible for the satisfactory completion of a job or they may be legally obligated to compensate the hiring firm for failure to complete.

### **Economic Realities Test**

A worker is an employee if he/she is a member of a class of workers intended to be protected by a law designed to protect or benefit employees.

### **Smell Test**

Takes into account totality of circumstances. Designed to foreclose efforts to artificially structure a relationship to circumvent the applicable criteria.

## **Helpful Tips**

- Watch out for independent contractors who are former employees performing the same job as before.
- Watch out for independent contractors who are doing the same job as employees.
- Don't rely on industry practice to protect your institution.
- If you think your independent contractor will never claim to be an employee, think again!
- Your PI's working relationship with an independent contractor should be based on the terms and conditions of their contract. Don't use the human relations department or the institution's personnel policies to resolve problems. If you have a problem, modify the contract.
- Don't invite independent contractors to employee functions.
- Try to minimize independent contractors' contact with funding agencies, etc.
- Keep independent contractor records in vendor files, not employee files. Require invoices.
- Work with your institution's legal office to develop policies and procedures.