

Independent Contractor Classifications Issues Coming Under Greater Scrutiny

The independent contractor “issue” has become more visible in the last year, as there seems to be growing momentum for Congress to act to stem abuses. Several states have also taken action to apply pressure to companies to revisit their classifications. It’s a subject that will likely see even more attention in the future. Legislators have heard an increasing number of complaints about misclassifications, and governments are looking for more revenue. Consequently, it’s more important than ever that organizations avoid misclassifying employees as independent contractors. Some suggest that somewhere from 10-30% of workplaces have misclassified their employees.

Independent Contractors A Money Saver and a Great Employer Solution?

The use of independent contractors has increased significantly in the last few years as employers seek to reduce costs and keep their workforces flexible. It’s been estimated that as much as 7% of the U.S. workforce is treated as independent contractors. Whether a worker is an employee, or a self-employed independent contractor, imposes very different obligations on an employer. Independent contractors are not on the payroll, and do not enjoy many of the legal protections and benefits given employees. They also typically don’t count toward minimum thresholds required to determine whether employers are covered by certain federal employment laws. Generally, employers are not required to:

- Provide Employee Insurance, Retirement and Leave Benefits
- Pay Social Security & Medicare Taxes
- Pay Federal & State Unemployment Taxes
- Pay Overtime or Minimum Wages
- Maintain Pay Records Under the FLSA
- Pay Worker’s’ Comp Premiums
- Provide protections under Title VII, the ADEA, ADA, and Other Discrimination Acts
- Provide protections under The National Labor Relations Act (which involves union issues)
- Provide Leave Under the FMLA

Or, A Business Decision That Can Have Significant Negative and Costly Consequences...?

It is often difficult to determine whether an individual should be classified as an employee or as an independent contractor. Some organizations incorrectly assume that they can “declare” an individual as an independent contractor, and that such a declaration will make it so. But as with all things HR related, nothing is simple. Failure to make a legally correct contractor vs. employee determination can lead to serious and expensive consequences. The issue typically arises because of a government audit or an employee complaint.

Or, A Business Decision That Can Have Significant Negative and Costly Consequences (Continued)

Too many organizations have ignored this issue (admittedly there are more interesting things to think about!). Others have simply tried to save money by not following the law. Unfortunately, some of them have paid a high price for doing so.

In any event, it may be a good time to refamiliarize yourself with the law and with the various tests swirling around the independent contractor issue. Then examine your own contractors, audit your company's practices, and take steps to assure future compliance.

How Do You Know if You Have an Independent Contractor?

Legal tests and factual situations, not labels, determine whether someone is a contractor or an employee. Simply calling someone an independent contractor and having him sign a contract to that effect is not controlling. A number of details about the work relationship must be analyzed.

And...To Make Things More Confusing, There Is More Than One Test

Several different tests (*Common Law*, *IRS Factor Control*, *Relative Nature of Work*, *ABC*, and *Economic Reality*) are used to determine independent contractor status under federal and state law. Which test is used depends upon the particular statutes or government agencies involved. No single factor is determinative of independent contractor status. However, the tests do have some significant similarities, with some of the main issues being:

- The degree of control exercised by the employer. Does the company control how the work will be performed (in which case you've likely got an employee) or, does the company simply oversee the result (which would be more favorable to a finding of an independent contractor relationship).
- Does the individual work independently or, is he regularly subject to supervision?
- Is the work performed on an ongoing basis?
- Is the work performed an integral part of the employer's business?
- Does the individual use company equipment and materials?
- Is work done at the company location and/or performed according to a schedule established by the company?
- How skilled is the individual? Does she have her own business? Does she have her own assistants?
- Does the individual incur his own profit or loss and cover his expenses?
- How is the individual paid? Does she set her payment rate? Is an invoice sent?
- Does the individual provide similar services to other organizations?

What Should You Do Now?

Using independent contractors inappropriately can create significant risks and liabilities. Review the law and the various contractor tests. Then examine your own contractors, audit your organization's practices, and take steps to assure future compliance. If you use independent contractors, use contracts. Finally, remember the "duck rule (if it looks like a duck and acts like a duck....") Sometimes no matter how you try to structure or "dress up" a relationship you've still got an employee.

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