

HOW TO DETERMINE WHO IS AN EMPLOYEE OR A SUB CONTRACTOR

The world is changing. The world of work is changing. While that has always been the case, we are feeling the effects more now than in any other time in our history. With the current recession, the new health care regulations, and work-life issues affecting everyone, including a rise in unemployment, we are feeling the pinch from employers asking for more work from fewer people. Additionally, companies are turning towards using contractors instead of employees as a way to reduce costs. This makes sense. Contractors do not have to be given benefits, thus passing on those costs to the contractor to manage.

In addition, many people who used to be employees are turning to contracting as a way to earn a living. According to the Bureau of Labor Statistics, approximately 679,000 new businesses were started in 2015. The owners of these businesses need to be sure of the regulations not only for tax purposes, but also for legal ramifications of responsibility of outcomes. The line between what constitutes an employee and a contractor is a fine one. Knowing the difference between what determines whether someone is a contractor or an employee is determined.

According to the Internal Revenue Service, the main issue determining the classification is control and independence. The degree of control and independence fall into three categories:

The first category is Behavioral. The questions to ask is whether the company controls or has the right to control what the worker does and the

method by which the worker does his or her job. It is important to know who determines the following:

1. When and where the work is done.
2. What tools or equipment are to be used to get the job done.
3. What people are hired to complete the work.
4. Where the supplies and services are purchased.
5. If a particular individual performs certain job tasks.
6. The order of the steps to follow when complete a task or tasks.

The second category is financial. This means that an employer would determine how the person doing the work is paid, if their expenses are reimbursed, and would supply the tools and materials to do the job. If the person doing the job has made a significant investment in the tools and equipment to be used in completing the work and the person doing the work has unreimbursed expenses, they face a greater chance to lose money on the job. The potential to lose money on the work indicates that the worker is an independent contractor.

In addition, if the person doing the work is free to seek out business opportunities, they may be considered an independent contractor.

The final category is the type of relationship that exists between the parties. If there are written contracts or employee type benefits (i.e. pension plan, insurance, vacation pay, etc.), there may be an employer and employee relationship. If the relationship is likely to continue and the work being performed is a key aspect of the business is indefinite, the worker is considered an employee.

So, what happens if a company classifies an employee as a contractor when they should not have? The employer may be liable for employment taxes for that worker, as well as any penalties that could be involved.

However, if an employer can demonstrate a reasonable reason for not treating a worker as an employee, they may not have to pay employment taxes for that worker. If this situation applies to you, you can get relief by filing the required federal information returns on a basis consistent with your treatment of the worker. In addition, you must not have treated any worker holding a substantially similar position as an employee for any periods beginning after 1977.

The rules for whether to classify someone as an employee or as a contractor can be confusing. However, be not afraid. Diligent research into what is required for either classification can clarify actions to be taken and questions to be asked. There are actions that can taken to be sure all laws and regulations are followed. If you have questions, be sure to consult a CPA or attorney with knowledge in this area. We advise that you think through the options, and are available to walk you through, and aid with, a determination if you need to reconsider how you are classifying the people who are performing the tasks to be done in your business... We enjoy helping our clients build their businesses, and would love to help you with yours.

Need Help Making This Decisions?

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