



INDEPENDENT CONTRACTOR CLASSIFICATION



After a long recruitment process, you've finally found a provider willing to sit down and review details of employment with you. You are thrilled to be on the same page regarding compensation, schedule, and treatment philosophy. There's just one catch. They tell you they'd like to be an independent contractor.

"I got a 1099 at my last job." "I make more money this way." "I don't want the benefits anyway, I'd rather have the cash." "I thought the compensation package we discussed was if I was withholding my own taxes?"

What do you do? You've already invested time and effort into this candidate, right? Doesn't it make sense to just say yes to the 1099?

DO NOT PASS GO. DO NOT COLLECT \$200.

Time and time again, we see our members succumb to the same mistake – they make a conclusion about whether to classify someone as an independent contractor or employee without fully analyzing the facts of the situation. And we get it! It's tempting to go with the flow, especially when you're trying to recruit valuable talent for your business.

The problem is, you cannot start at the conclusion and work your way backwards from there. Much like a board game, employee versus independent contractor analysis requires that you work "Start to Finish" (not "Finish to Start"). In other words, you must start at "Employee" and work your way through each factor of the analysis to see where you land. Why do we use "Employee" as our starting point? Because "employee" is the default rule. Independent contractors are the exception, not the rule.

AND THE BANKERS ACTUALLY CARE IN THIS GAME...

Unlike your 8-year-old nephew who may play a little fast and loose with those fake dollar bills, the IRS and state/federal Departments of Labor do care about employee misclassification. The IRS wants to see that you're withholding taxes properly, including employee-specific taxes like Social Security. State and federal labor agencies want to ensure that employees are receiving the rights and benefits of employment required by law – Social Security contributions, health insurance, workers' compensation, disability accommodation, required paid sick leave, leaves of absence, and more. Failure to classify workers correctly can result in fines, penalties, back wages, and potentially litigation.

And while these agencies care quite a bit about collecting their money and enforcing employee rights laws, one thing they certainly do not care about in this analysis is whether the worker agreed to be classified as an independent contractor. That's right! **Saying that the worker requested or agreed to be an independent contractor is not a defense.** The responsibility of legal compliance falls squarely on the shoulders of the employer, read: you.

What does a consequence look like? Let's look at a common example of a worker misclassified as an independent contractor. This worker is injured in your office when they burn their hand on a hot piece of equipment. They do not carry their own health insurance, or workers' compensation insurance. What's more, they do not have any sick days or other time off benefits. They become upset when they realize that your workers' compensation plan only covers employees, not independent contractors. After realizing the injury is going to keep them from working for some time, they seek a local attorney to see what they can do. The local attorney recognizes that you've misclassified this worker, and you are now being sued not only to extend workers' compensation coverage to this worker, but for back wages, benefits, and all other benefits of employment.

THE RULES OF THE GAME.

One of the challenges with proper independent contractor classification is the fact that there is not one set of rules to play by. While generally the analysis falls into the three main categories outlined below, the IRS and DOL each have their own tests, and state agencies often apply even more strict standards (looking at you California and New Jersey). The three main considerations, and examples of factors falling into each category, are as follows:

- **Behavioral Control.** How much control and direction do you expect to have over the worker's duties? The more you care about the means rather than the ends, the more likely it is that the worker is an employee. Compare this to when you hire an IT person as a contractor to perform maintenance on your computer systems. You probably don't care how the job is done as long as your systems are working.
 - Contractors set their own hours, meaning they can schedule patients according to their own schedules.
 - Contractors bring some or all of their own tools and/or employees.
 - Contractors use their own techniques, plans, methods, and skills. If they treatment plan differently than you do, that's OK. If they use a different software system than you do, that's OK.
 - Contractors have the freedom to work for other businesses. It is rare to have a non-compete with an independent contractor, as you typically expect that they would be providing similar services to different businesses. Therefore, this should not be viewed as a threat to your business.

- **Financial Control.** How dependent is the worker on you as their source of income? Does the worker perform the same service for a variety of businesses, or are you their only "customer?" Do you pay the worker a flat fee for the job, or do you pay them an hourly rate like your other employees? Does the worker have "skin in the game", with the ability to realize profit and loss?
 - Contractors are not solely reliant on you for income. They perform similar services for different businesses, just like any other service company (e.g. IT company, cleaning company).
 - Contractors have the ability to realize profit or loss, meaning you do not typically guarantee them a base salary, provide paid time off, or guarantee a minimum number of patients.

- **Relationship of the Parties.** Is the worker engaged for a limited project or defined period of time; or are you in a relationship indefinitely? Does the worker supplement tasks performed by your normal staff, or are they performing work that you would otherwise be referring to a third party?
 - Contractors are performing work that is different from the normal work of your business. This could be work that you would otherwise be referring out, or a specialized service comparable to that of an IT company or cleaning service.
 - Contractors are engaged in a limited project, or for a limited period of service. The broader and more undefined the scope of the work and services performed, the less likely it is that a worker is an independent contractor.

As you can see, the analysis quickly becomes complex and multi-faceted, which underscores the importance of actually performing the analysis for each working relationship. A full copy of the [IRS's 20-factor independent contractor test](#) is attached to the end of this guide, and we encourage you to use it as you assess your relationships.

LET'S PLAY A PRACTICE ROUND.

Before you are faced with a decision where real dollar bills are on the line, let's play a round with some paper money.

GEMS GENERAL MEDICINE, LLC

In the first example, you are the owner of a general medical practice. You are seeking an associate doctor to assist with patients, and take some of the burden off of you when answering emergency calls and scheduling appointments. Gwen, a general practitioner, replies to your job ad, and she seems like the perfect fit. You discuss with her that you will supervise and train her, and that she will take on a portion of your current patient base, as well as a portion of your new patient base. Gwen is interested in full-time employment with your business, and will not be working elsewhere while working for you.

Is Gwen an Independent Contractor or Employee?

Gwen is an employee. You wish to have control and direction over her work. Her work is supplementing the work your business already does, meaning she is performing the normal work of your business. Gwen will only be working for you, and is not customarily engaged in an independently established business of her own.

GREAT GRINS, LLC

In the second example, you are the owner of a general dental practice. Recently, you have had several patients express that they would prefer to receive specialty endodontic treatment (aka root canals) in the comfort of your office, rather than having to drive across town to an unfamiliar practice. Since you are not a trained endodontist, you seek a qualified endodontist to come in once per month to treat your patients who are in need of endodontic work. George, an endodontist, replies to your job ad. He is only available on the third Friday of every month because he travels around to different businesses all over the area to do specialty treatment. George owns his own business, George I. Drill, LLC, where he employs a part-time scheduler and a full-time assistant. He will bring his own staff and tools when he visits your office, and he will be responsible for monitoring his own quality of care and completing his own treatment planning and records.

Is George an Independent Contractor or Employee?

George is likely an independent contractor. You will not be directing his work, and you would not offer this service to your patients in the ordinary course of your business. George regularly performs work for other businesses of this same nature, and he has an independently established business of his own.

COMFORT CHIROPRACTIC

In the third example, you are the owner of a chiropractic practice. You are seeking to expand your business in order to offer more services to your patients, such as massage or acupuncture. You know you only have the resources to bring other professionals into your office on a part-time basis to start. Your long-term goal is to expand your business into an integrative health center, where patients can seamlessly schedule treatment with a variety of professionals. You are looking for partnerial relationships to help your business grow. Chris, a licensed massage therapist, replies to your ad. Chris is finishing his bachelor's degree in business, and wishes to work part-time until he graduates, at which point he is interested in taking on more work with your business.

Is Chris an Independent Contractor or Employee?

While it's a tough call, Chris is best classified as an employee. There are facts here to support both independent contractor and employee status, thus, the most conservative classification is as an employee.

While you may not have control over the techniques he uses as a massage therapist, you are looking for a partner to grow your business (rather than a contractor for services). This situation can be contrasted with a situation where a massage therapist “rents a room” from a business. While massage therapy is not currently something your business offers, the goal is to integrate different services into your model, and to centralize those services within your business. Chris does not have his own business and seeks to contribute more than just a massage therapy service to your team with his business degree.

KEEP MR. MONOPOLY’S MONOCLE AT BAY

No business wants to be faced with an audit or other unnecessary scrutiny. So how can you show that you’re playing a clean game?

First, perform a full analysis on any worker you’re considering classifying as an independent contractor. If you decide contractor is the correct classification, ***maintain documentation to support this determination***. Keep the worker’s employer identification number (EIN), business information, independent insurance, invoices, and the like in your files. An independent contractor agreement can help clear up issues like whether the worker will be bringing their own staff, equipment, and how the worker will be paid.

Second, if you’re doubting classification, you may work with your accountant to request an IRS Determination of Worker Status for Purpose of Federal Employment Taxes and Income Tax Withholding. Your accountant can help you file a Form SS-8 in order to request a determination. Note that a decision from the IRS may provide peace of mind for tax purposes, but does not have any bearing on the applicability of other labor laws.

Finally, if you have already misclassified someone as an independent contractor, work carefully with professionals if you are thinking of switching them over to employee status. Anytime the IRS sees a 1099 and a W-4/W-2 filed for the same individual in the same taxable year, this can flag your business for an audit. You may choose to transition the worker at the beginning of a taxable year to avoid this issue, and should discuss pros and cons of this decision with your tax professional.

THIS IS TAKING FOREVER...

We know, we know. We’re several pages into this Monopoly analogy, and just like the real game, independent contractor analysis does take quite a bit of time to explain. What you need to remember is that you should never assume that it’s fine to classify someone as an independent contractor – do a full analysis each and every time. And as always, contact CEDR with any questions or concerns about your compliance in this area.



INDEPENDENT CONTRACTOR CHECKLIST

Employers may use the following checklist to classify individuals as independent contractors. If more than 3 questions are answered yes, it is likely the person would be properly classified as an employee instead. Contact the CEDR Solution Center if you still have questions (866) 414-6056.

Factors which show control	Yes/EE	No/IC	N/A
1. Worker must comply with instructions on how to do their job.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
2. Worker is trained by person hired.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. Worker cannot hire or fire his or her own assistants.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
4. Work relationship is continuous or indefinite.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
5. Work hours are preset by the business.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
6. Worker must devote full time to this business.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
7. Work is done on the employer's premises.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
8. Worker cannot control order or sequence of work.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
9. Worker is paid at specific intervals.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
10. Worker's business expenses are reimbursed.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
11. Worker is provided with tools or materials.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
12. Worker has no significant investment in performing his/her services.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
13. Worker has no opportunity for profit/loss.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
14. Worker is not engaged by many different firms; or is required to work only for the one company.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
15. Worker does not offer services to public, nor advertises the services he or she provides.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
16. Worker may be discharged by employer without penalty.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
17. Worker is paid directly, not to the worker's company.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
18. Worker is provided benefits such as vacation, pension plan, and bonus.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
19. Worker is required to sign the Employee Handbook, W-4, or other Employee forms.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
20. Worker provides services that are a key aspect of the business.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>



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