

Worker Classification and Taxes: What You Need to Know

Jessie G. Campbell

Director, Low Income Taxpayer Clinic



Education Presentation

Disclaimer: This presentation is intended to be for information and educational purposes only. If you have any questions about your specific legal situation, we recommend that you contact an attorney.



What is Worker Classification?

- Types of Classification (people who work for you)
 - Employee
 - Independent Contractor
 - Professional
- It is basically deciding what laws apply to the person that is doing work for you.



How to Determine

- **Common Law** – Focuses on whether an employer has control over that manner and means by which services are performed by the worker.
- **Economic Realities** – Focuses on whether the worker is a business owner.
 - Fair Labor Standards Act (FLSA)
 - Equal Employment Opportunities (EEO)
 - States
- **Statutes – Law** – Congress has determined that regardless of the other tests, the worker is a specific type for that law's purpose.



Why It Matters?

- **Federal Insurance Contributions Act (FICA) – Taxes**
- *Federal Unemployment Act (FUTA)*
- Worker's Compensation
- Fair Labor Standards Act
- Social Security Act
- National Labor Relations Act
- Title VII of Civil Rights Act
- Equal Pay Act
- Age Discrimination in Employment Act
- Family and Medical Leave Act
- Americans with Disabilities Act
- Immigration Reform and Control Act
- State Laws



Taxpayer Bill of Rights

- To be Informed
- To Quality Service
- To Pay No More than the Correct Amount of Tax
- To Challenge the IRS's Position & Be Heard
- To Appeal an IRS Decision in an Independent Forum
- To Finality
- To Privacy
- To Confidentiality
- To Retain Representation
- To a Fair and Just Tax System



IRS – Worker Classification

- Effect of Being an Employee for IRS purposes – affects who is responsible for taxes.
- IRS – Two Tests
 - Statute
 - Common Law Test
- Who Gets to Decide?
 - Form SS-8



Statute – Employee

- An agent (or commission) driver who delivers food, beverages (other than milk), laundry, or dry cleaning for someone else.
- A full-time life insurance salesperson who sells primarily for one company.
- A homemaker who works by guidelines of the person for whom the work is done, with materials furnished by and returned to that person or to someone that person designates.
- A traveling or city salesperson (other than an agent-driver or commission-driver) who works full time (except for sideline sales activities) for one firm or person getting orders from customers. The orders must be for merchandise for resale or supplies for use in the customer's business. The customers must be retailers, wholesalers, contractors, or operators of hotels, restaurants, or other businesses dealing with food or lodging.



Statute – Nonemployee

- Direct sellers
- Qualified real estate agents
- Certain companion sitters – Not employees of a companion sitting placement service



Common Law Test – 3 Categories

- **Behavioral Control** covers facts that show if the business has a right to direct and control what work is accomplished and how the work is done, through instructions, training, or other means.
- **Financial Control** covers facts that show if the business has a right to direct or control the financial and business aspects of the worker's job.
- **Relationship of the Parties** covers facts that show the type of relationship the parties had.



Common Law Test – 20 Factors

- Instructions
- Training
- Integration
- Services Rendered Personally
- Hiring, Supervising, and Paying Assistants
- Continuing Relationship
- Set Hours of Work
- Full Time Required
- Doing work on Employer's Premises
- Order or Sequence Set
- Oral or Written Reports
- Payment by Hour, Week, or Month
- Payment of Business and/or Travel Expenses
- Furnishing of tools or materials
- Significant Investment
- Realization of Profit or Loss
- Working for More than One Firm at a Time
- Making Service Available to General Public
- Right to Discharge
- Right to Terminate



Income Tax

- Income Tax = Pay-As-You-Go Tax
- Employee – Employer Responsible
 - Withholding Taxes
 - Complete Form W-4
- Independent Contractor – Worker Responsible*
 - Estimated Taxes
 - Quarterly Basis
- * Exception – Nonresident Aliens – Subject to 30% withholding for Independent Services Performed



Social Security and Medicare Tax

- First Half – every worker is responsible, regardless of classification
- Who is Responsible for Second Half? Two Laws:
 - Federal Insurance Contributions Act (FICA) – Employer
 - Self-Employed Contributions Act (SECA) – Independent Contractor



Treating Employees as Nonemployees

- Subject to Employment Tax Audit
- Penalties and Liabilities
 - Depends on whether Forms 1099 were filed.
 - Still liable for income tax withholding even if the taxes were paid by the employee.
 - Still responsible for employer's portion of FICA taxes.



Settlement Options

- **Classification Settlement Program (CSP)**
 - Under an employment tax audit
 - With a few exceptions, it is mandatory that the Service make a CSP offer.
 - Binding for IRS and taxpayer-business
- **Section 530 Safe Harbor – Potential Relief**
 - Must prove it has a reasonable belief for treating its workers as independent contractors.
 - Must prove that it treated all of its workers in a similar situation the same (substantive consistency).
 - Must have filed all required tax filings (for example, Form 1099-MISC) (reporting consistency).



Voluntary Reclassification

- Voluntary Classification Settlement Program
 - Opportunity to reclassify workers and employees who are being treated as independent contractors or other nonemployee.
 - Cannot be under an employment audit
 - Results
 - 10% of employment tax liability
 - Not liable for interest and penalties on that amount
 - Not subject to employment tax audit for those workers for prior years
 - Request – Form 8952



Thank You

