

The Top Common Misconceptions of Independent Contractors

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Year in and year out I read about companies getting fined over misclassifying employees as Independent Contractors. We even help our clients deal with these issues. This type of behavior is more common than not. While on the phone with California Employment Development Department (EDD) yesterday, I asked the auditor about his experiences dealing with companies misclassifying employees as independent contractors. When I tell you this, you might not believe me, but I kid you not. He told me a story about a company that made everyone, from the receptionist to the CFO as an independent contractor. The owners reasoning for this was that every person is responsible for their own work and they can quit whenever they want. MISCONCEPTION! I was shocked that someone would honestly believe that was accurate, but as a prior Director of HR and HR Consultant you seem to not get surprised about peoples thought process on labor law and HR issues. I believe he had the at-will employment law mixed up with the guidelines of independent contractors. Just my thoughts.

I thought I'd put together the most common misconceptions about Independent Contractors for employers. Something easy to reference to when they have doubt, but always remember to seek legal help when trying to classify independent contractors and you should have, if not already an Independent Contractor agreement, independent contractor checklist and our [“How Six Agencies Determine Relationships”](#) guide. This will help you further clarify who and who's not an Independent Contractor. Your agreement should be developed by one of our employment law lawyers or any employment law lawyer. **I am not a lawyer**; just an HR professional with over 15 years of experience. **So there is my disclaimer.** In bold so you don't miss it.

I know you decided to read this article about the common misconceptions, not me babble on and on. So let's jump right into it.

Here are the 9 most common misconceptions:

1. *If I issue an Internal Revenue Service (IRS) Form 1099-MISC, then the worker is an independent contractor.*

NOT TRUE. An IRS Form 1099-MISC is simply a method the government uses to track and report certain types of nonemployment income. When you provide an IRS Form 1099-MISC to a worker for payment of services, it does not automatically make the worker an independent contractor.

2. *If I pay a worker less than \$600 in a year, then the worker is not subject to California payroll taxes.*

NOT TRUE. The amount paid to a worker is not, by itself, a factor in determining whether a worker is an employee or independent contractor. The amount paid to a worker may determine if you should issue an IRS Form 1099-MISC. For information on the federal requirements, access the IRS website at www.irs.gov or contact the IRS at (800) 829-1040.

3. *The part-time, temporary, probationary, and substitute workers I employ are day laborers or casual laborers, not employees.*

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NOT TRUE. An employee may perform services on a less than full-time permanent basis. The law does not exclude services from employment that are commonly referred to as day labor, part-time help, causal labor, temporary help, probationary, or outside labor.

4. *If a family member works for me, he/she is not an employer.*

NOT TRUE. Family members working for your business are employees and subject to California payroll taxes unless certain conditions are met.

5. *My worker and I have signed a written that makes my worker an independent contractor.*

NOT TRUE. A written contract or agreement does not necessarily depict the actual relationship. The actual practices of the parties in a relationship are more important than the wording of an agreement in determining whether a worker is an employee or independent.

6. *My competitors treat their workers as independent contractors; therefore, it is okay for me to treat my workers as independent contractors.*

NOT TRUE. The law defines employment relationships, not you or the actions of your competitors. If you misclassify your workers as independent contractors, EDD may assess you for the unpaid payroll taxes for any unreported employees.

7. *My worker performs similar work for other businesses, so the worker is an independent contractor.*

NOT TRUE. Performing similar work for other businesses is not, by itself, a determining factor. The relationship the worker may have with the other businesses is not controlling factor when determining the worker's status as an employee or independent contractor with your business. The working relationship with each business is looked at separately.

8. *My worker has a city business license and business card, so the worker is an independent contractor.*

NOT TRUE. A city business license and business card, by themselves, do not make a worker an independent contractor. All of the common law factors need to be reviewed and weighted with the respect to the specific circumstances of the services provided by each worker.

9. *I pay my workers solely by commission; therefore, they are independent contractors.*

NOT TRUE. The method of payment is not, by itself, a determining factor. All of the common law factors need to be considered and weighted to determine whether a worker is an employee. If the worker is an employee, then all remuneration for services (salary, hourly pay, piece rate, commissions, bonuses, stock options, vehicle, etc) is wages.

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We have just identified the most common misconceptions for independent contractors and as you can see a lot of employers and HR professionals deal with these misconceptions everyday. You were probably thinking to yourself while reading this, oh yeah I have thought of some of those misconceptions. Don't worry, a lot of people think that those are valid reasons to make someone an independent contractor. You are not alone. That's why I am here to help.

Here is another way to identify an individual from an employee. EDD describes an individual from an employee by this description. “**An individual is an employee** when hired by an employer to perform services and either (1) the law defines the worker as an employee (statutory employee) or (2) the employer has the right to control the manner and means by which the worker performs his/her services (common law employee).”

What Next?

So we have talked about the common misconceptions and how EDD describes an individual from an employee. Employers and HR professionals need to remember, that there is not a set definition of the terms “independent contractor” for all purposes. The issue of whether a worker is an employee or independent contractor depends on the particular area of law to be applied. The right to control the manner and means by which the individual performs his or her services is generally the most important factor, however. You have to look at the interpretations of the various enforcement agencies and the courts to determine if a worker is an employee or an independent contractor in any given situation. For example, in a wage claim where employment status is an issue, the Division of Labor Standards Enforcement (DLSE) will often use the five-prong economic realities test to decide the issue.

However, in a separate matter before a different state agency with the same parties and same facts, and employment status again being an issue, that agency may be required to use a different test, such as the control test, which may result in a different determination.

It is possible that the same individual will be considered an employee for purposes of one law and an independent contractor under another.

The consequences for misclassifying an employee as an independent contractor can include significant tax, wage and benefits liabilities, as well as massive fines that the IRS and the EDD may impose.

Because different tests may apply, and because the potential liabilities and penalties are significant if the individual is misclassified as an independent contractor, each working relationship must be thoroughly researched and analyzed. You should assume all workers are employees unless they clearly meet all legal requirements and pass all tests various federal and state agencies use for proper classification of independent contractors.

State and federal agencies use their own tests to determine if an individual qualifies as an independent contractor. Understand them all before classifying an individual as an independent contractor. Consultation with legal counsel is usually warranted.

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It is unlawful for any person or employer to "willfully misclassify" an individual as an independent contractor.

Willful misclassification means: "avoiding employee status for an individual by voluntarily and knowingly misclassifying that individual as an independent contractor."

The civil penalty for violation of this law ranges from \$5,000 to \$25,000 for each violation. Other remedies include requiring the employer to display on its website or in the workplace a notice of the serious violation of misclassifying an independent contractor, a statement that the employer has changed its business practices in order to comply with the law, and information on how to contact the Labor and Workforce Development Agency to report misclassification. The notice must be posted for one year, and signed by an officer of the employer.

For your own protection, make sure that a person working as an independent contractor truly meets the difficult tests required by law.

Closing

That was a lot to cover for just some common misconceptions, but I hope this whitepaper will help you have a better understanding about what and what not constitutes an Independent Contractor. Please feel free to pass this on to whomever you think can benefit from this.

In either case, the principles outlined in this white paper should help you avoid some of the most common misconceptions of independent contractors. If you would like more detailed information regarding Independent Contractor vs. Employee, check out our [podcast page](#). We add a new podcast every Wednesday about a specific HR or labor law issue. While there, check out our [blog](#).

HR Allen Consulting Services Can Help!

We hope that you found this information helpful. If you have questions about classification of Independent Contractors vs. Employee or would like to learn more about our tools and resources, please call us at (888) 353-2976, Monday through Friday, 8:00 a.m. to 5:00 p.m.

About HR Allen Consulting Services

HR Allen Consulting Services is a full-service HR and Payroll company offering small and medium sized businesses with reliable payroll and HR Management and business services. Since 2005, we have grown to be the premier choice for payroll and HR services by business owners and HR professionals throughout California, Nevada and Arizona. We have also been voted "Best Human Resource & Payroll Company" for 2011 by the City of Citrus Heights.



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Sources:
California Employment Development (EDD)
California Chamber of Commerce