

# Hiring Considerations

## Employee vs. Independent Contractor

It is important for any business to understand the difference between an "employee" and an "independent contractor," and to make sure that each is treated in an appropriate manner because of the potential for financial penalties. A business that erroneously categorizes an employee as an independent contractor may be liable for withholding income taxes, withholding Social Security and Medicare taxes, payment of unemployment taxes on wages, payment of worker's compensation insurance, and possible penalties ("Employment Taxes"). This is because a business is responsible for such Employment Taxes. The same is not true for a business that uses independent contractors. An independent contractor is responsible for accounting for and payment of their own income taxes, and Social Security and Medicare taxes.

Because of the financial implications, the Internal Revenue Service and the State of Maryland heavily scrutinize whether businesses properly treat their workers as employees or independent contractors. Generally speaking, the test used to determine whether a worker is an employee or an independent contractor is whether or not the business controls the services to be rendered.

The concept of "control" includes behavioral control, financial control and the relationship between the parties. The concept of behavioral control requires an employer to direct or control the services provided by the worker through instructions, training or other means. Financial control means that the employer directs or controls the financial and business aspects of the worker's job. For example, an employer with financial control over a worker may determine how the worker's business expenses are reimbursed, how the worker makes his/her services available to the industry, how the worker is paid and whether the worker realizes profits and losses. The relationship of the parties should be clearly defined.

Often, it is useful for the business to memorialize the relationship between the business and the worker in a written contract which describes the relationship between the parties as either an employer/employee relationship or independent contractor relationship, and further describes other aspects of the relationship such as, whether the worker may perform similar services for other businesses, the nature of any benefits provided by the business (insurance, vacation, etc.), and the duration of the relationship. It is important to keep in mind, however, that merely stating in a contract that a worker is an independent contractor is not in itself the defining factor.

In an effort to assist businesses, the Internal Revenue Service has developed a series of guidelines for businesses to follow to determine whether a worker is an employee or an independent contractor. Some of these guidelines include:

- whether the services performed by the worker are integrated into the business' operations;
- whether the services must be rendered personally by the worker;
- whether the business dictates the hours and schedule of the worker;
- whether the worker provides services to the business on a full-time basis;
- whether the worker provides tools, materials and equipment; and
- whether the worker makes his/her services available to the public.

Two examples highlight the difference between an employee and independent contractor.

In the first example, a worker is hired by a construction company. The worker works on a full-time basis installing dry wall. The worker takes direction from the construction company's foreman, who assigns the worker to various construction projects. The worker gets paid on a bi-weekly basis by the company and receives health care benefits, vacation pay and participates in the company's pension plan. The worker is an employee.

In the second example, a consultant advises a development company on various land acquisition opportunities. The consultant also advises several other companies. The development company only uses the consultant's services when it wants to purchase and develop land, and pays a fee to the consultant on each purchase. The consultant works out of her home, on a part-time basis, dictates her own schedule and requires the company to sign a separate contract for each purchase. The consultant is an independent contractor.

Each business is unique, and compliance with the guidelines discussed in this article can be a complex and ambiguous process. Because the financial consequences of erroneously treating an employee as an independent contractor can be severe, each situation must be examined separately. If you have questions about how your business is treating its workers, you should discuss the issue with your accountant or your lawyer. ■

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EMPLOYEE'S PERSONNEL FILE\*

NAME  
BY DAVID B. APPLEFELD, ESQ.  
AND SHOBITA C. DUBOIS, ESQ.

PRINT EMPLOYEE'S NAME ON

ADDRESS INFORMATION

DATE ADDRESS

CHECK

APPLICANT

GENERAL INTERVIEW

INTERVIEWER

DEPARTMENT SUPERVISOR

1st Interview

After the interview, check the

JOB EXPERIENCE

Applicant has Strong

EMPLOYMENT INTERVIEW

