

INDEPENDENT CONTRACTORS IRS 20-FACTOR TEST

An independent contractor is a worker who individually contracts with an employer to provide specialized or requested services on an as-needed or project basis. This individual is free from control and direction of the performance of their work, and the individual is customarily engaged in an independent trade, occupation, profession, or business.

Independent contractors have greater control over the way they carry out their work than employees. Employers assume fewer duties with respect to independent contractors than employees.

Independent contractors are generally outside the coverage of various laws that apply to the employer-employee relationship. An employer must exercise extreme caution when classifying a worker as an independent contractor. This is especially important when it comes to issues such as pension, workers compensation, and wage and hour law. Employers do not withhold federal, state and local taxes from wages paid to independent contractors, they are not included in an employer's benefits programs, are exempt from wage and hour, employment discrimination laws and unemployment insurance. Therefore, the penalties for misclassifying a worker can be huge. Penalties can include back taxes or premiums, civil fines, interest, and other retroactive damages.

The independent contractor relationship is beneficial to both parties, so pursuing an independent contractor arrangement is a practical way to do business for employers. The IRS has developed guidelines to help the employer to correctly classify their employment relationships. The IRS follows the common law test for determining whether an individual is an employee for federal employment tax purposes. Under the common law test an employer-employee relationship exists if the person for whom services are performed has the right to control and direct a worker in results, specific details and the means by which the results are accomplished.

The "Reasonable Basis" test provides a "safe harbor" to employers, which bars the IRS from challenging the status of workers as independent contractors if certain conditions are met. If the following conditions are met the employer does not have tax liability for workers under Section 503 and the IRS cannot penalize an employer for misclassifying a worker as an independent contractor:

- The employer has always treated the worker as an independent contractor
- The employer has filed all returns for the worker for all periods after 1978 and the returns were consistent with independent contractor status
- The employer had a reasonable basis for treating workers as an independent contractor by either relying on judicial precedent, published rulings or technical advice, a prior IRS audit showing no penalties assessed for similarly situated workers, or a longstanding recognized practice of a significant segment of the industry in which the individual worked.

The IRS developed the 20-Factor Test shown below to help employers evaluate whether a worker is an employee or an independent contractor. No one factor on the test is more indicative of employee status than another. If there is a high number of "yes" marks, then it will most likely indicate the presence of an employment relationship, a high number of "no" marks may or may not indicate a contractor relationship. Therefore, it is best for employers to err on the side of caution and to pursue an IRS ruling when in doubt. The important thing to remember when evaluating the status is who has the right to control the work as to when and how it is completed.

Employers and workers should file Form SS-8 (Determination of Employee Work Status for Purposes of Federal Employment Taxes and Income Tax Withholding) to get a determination from the IRS as to whether or not a worker is an independent contractor.

The IRS has released a 123-page manual designed to provide guidance to employers. The manual simplifies and explains the 20-point test. For a copy of the manual, you can contact the IRS center nearest you.

IRS 20-FACTOR TEST		ÖCHECK YES OR NO
1. Instructions	Is the worker required to comply with employer's instructions about when, where, and how to work?	<input type="checkbox"/> YES <input type="checkbox"/> NO
2. Training	Is training required? Does the worker receive training from or at the direction of the employer, includes attending meetings and working with experienced employees?	<input type="checkbox"/> YES <input type="checkbox"/> NO
3. Integration	Are the worker's services integrated with activities of the company? Does the success of the employer's business significantly depend upon the performance of services that the worker provides?	<input type="checkbox"/> YES <input type="checkbox"/> NO
4. Services Rendered Personally	Is the worker required to perform the work personally?	<input type="checkbox"/> YES <input type="checkbox"/> NO
5. Authority to hire, supervise and pay assistants	Does the worker have the ability to hire, supervise and pay assistants for the employer?	<input type="checkbox"/> YES <input type="checkbox"/> NO
6. Continuing Relationship	Does the worker have a continuing relationship with the employer?	<input type="checkbox"/> YES <input type="checkbox"/> NO
7. Set Hours of Work	Is the worker required to follow set hours of work?	<input type="checkbox"/> YES <input type="checkbox"/> NO
8. Full-time Work Required	Does the worker work full-time for the employer?	<input type="checkbox"/> YES <input type="checkbox"/> NO
9. Place of Work	Does the worker perform work on the employer's premises and use the company's office equipment?	<input type="checkbox"/> YES <input type="checkbox"/> NO
10. Sequence of Work	Does the worker perform work in a sequence set by the employer? Does the worker follow a set schedule?	<input type="checkbox"/> YES <input type="checkbox"/> NO
11. Reporting Obligations	Does the worker submit regular written or oral reports to the employer?	<input type="checkbox"/> YES <input type="checkbox"/> NO
12. Method of Payment	How does the worker receive payments? Are there payments of regular amounts at set intervals?	<input type="checkbox"/> YES <input type="checkbox"/> NO
13. Payment of Business and Travel Expenses	Does the worker receive payment for business and travel expenses?	<input type="checkbox"/> YES <input type="checkbox"/> NO
14. Furnishing of tools and materials	Does the worker rely on the employer for tools and materials?	<input type="checkbox"/> YES <input type="checkbox"/> NO
15. Investment	Has the worker made an investment in the facilities or equipment used to perform services?	<input type="checkbox"/> YES <input type="checkbox"/> NO
16. Risk of Loss	Is the payment made to the worker on a fixed basis regardless of profitability or loss?	<input type="checkbox"/> YES <input type="checkbox"/> NO
17. Working for more than one company at a time	Does the worker only work for one employer at a time?	<input type="checkbox"/> YES <input type="checkbox"/> NO
18. Availability of services to the general public	Are the services offered to the employer unavailable to the general public?	<input type="checkbox"/> YES <input type="checkbox"/> NO
19. Right to discharge	Can the worker be fired by the employer?	<input type="checkbox"/> YES <input type="checkbox"/> NO
20. Right to quit	Can the worker quit work at any time without liability?	<input type="checkbox"/> YES <input type="checkbox"/> NO

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