



## **Update to IRS 20 Point Employee or Independent Contractor Test** *Carl Blankschaen, CPA*

For many years the IRS has used a twenty point test to determine if a worker should be classified as an employee or an independent contractor with respect to their employer. IRS Publication 15-A condensed the twenty points into eleven factors. In substance, these factors still evaluate a worker's status the same way as before. The evaluation is now concisely grouped into three categories: Behavioral Control, Financial Control, and the Type of Relationship Between the Parties.

The importance of determining an employer's workers as either **Employees** or **Independent Contractors** is that for **employees**, an employer must generally withhold:

- Federal Income Taxes
- Social Security Taxes
- Medicare Taxes
- Unemployment Taxes
- Additionally, during 2012, **Senate Bill 459** increased the penalty for employers who willfully misclassify employees as independent contractors. These penalties range between **\$5,000** to **\$15,000 for each violation**.

If a worker is classified as an **Independent Contractor**, the employer does not generally have to withhold or pay the above mentioned taxes.

The IRS determines a worker's classification based on the relationship between the worker and the business. There is no bright line rule test for this distinction. Instead, the IRS will weigh eleven factors grouped into three categories:

### A. Behavioral Control

1. Instructions that the business gives to the worker
2. Training that the business gives to the worker

### B. Financial Control

3. The extent to which the worker has unreimbursed business expenses
4. The extent of the worker's investment
5. The extent to which the worker makes his or her services available to the relevant market
6. How the business pays the worker
7. The extent to which the worker can realize a profit or loss

C. Type of Relationship Between the Parties

8. Written contracts describing the relationship the parties intended to create
9. Whether or not the business provides the worker with employee-type benefits, such as insurance, a pension plan, vacation pay, or sick pay.
10. The permanency of the relationship
11. The extent to which services performed by the worker are a key aspect of the regular business of the company

It is important to keep in mind that the above are only factors considered in the determination of a worker's status. There is no set number of the above factors that if met will classify a worker as an employee or independent contractor. The above are presented as guidelines for employers to make their own determinations.

For more information on Employee or Independent Contractor classification or if you have questions regarding this topic, please contact a Zinner and Co. nonprofit or tax professional.