Independent Contractor Workshop

Financial and Business Services

2010

Agenda

• Why is independent contractor/employee classification important
• What is the political emphasis on this area
• What happens when misclassified
• What are the factors of classification
• Policy and Procedures
• IRS independent contractor classification checklist

WHY IS CLASSIFICATION OF INDEPENDENT CONTRACTOR OR EMPLOYEE IMPORTANT?
IRS announced in 2009 that it will be focusing attention on whether a proper determination has been made to classify workers as employees or independent contractors and will be conducting 6000 audits.

Will IRS initiative affect the U?
- The IRS already reclassified two of U’s independent contractors to employees in 2009
- Back employment taxes owed plus interest
- Benefits issues
- Administrative resources

The IRS DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT STATED:
“The misclassification of employees as independent contractors is a nationwide issue affecting millions of workers that continues to grow and contribute to the tax gap.”
The IRS DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT (con’t):

"IRS research indicates that employers often misclassify workers as independent contractors for various reasons."

"These employers avoid paying their share of employment taxes as well as other expenses such as workers' compensation, unemployment insurance, and other benefits."

New York Times article Feb 2010

- The Obama administration assumes federal crackdown will yield $7 billion over 10 yrs
- Labor Department estimates 30% of employers misclassify employees
- Misclassification can deny workers' basic rights and protections

What happens if a worker is reclassified from Independent Contractor to Employee?

Can result from:
- worker complaint
- IRS audit
- interested party complaint
Employers who misclassify workers as independent contractors can end up with substantial tax and other bills.

- Penalties for failing to pay employment taxes
- Penalties for failing to file required tax forms
- Penalties for failing to pay workers comp and more
- Payment of FICA for both individual and employer
- Amended W-2s requiring amendment of tax returns
- May be retroactive benefits such as:
  - Retirement contribution
  - Health insurance coverage
  - Sick/vacation leave

Why Use Independent Contractors?

Good Reasons
- Specialized expertise needed
- Non-integral undertakings
- Short term projects
- Institution doesn’t have employees who do this job

Why Use Independent Contractors?

Bad Reasons:
- Payroll tax and benefit avoidance (i.e. the worker or employer doesn’t want taxes taken out)
- Circumvention of personnel rules and pay restrictions
- That is what the worker wants
What is an independent contractor?

- The IRS uses three characteristics used to determine the relationship between businesses and workers:
  - Behavioral Control
  - Financial Control
  - Relationship

1. Behavioral Control

whether the business has a right to direct or control how the work is done through instructions, training or other means

Behavioral Control-employee examples

- how, when, or where to do the work
- what tools or equipment to use
- what assistants to hire to help with the work
- where to purchase supplies and services
• if the business provides worker with training about required procedures and methods, this indicates that the business wants the work done in a certain way, and this implies **employee status**

**Behavior Control-independent contractor**

• If worker receives less extensive instructions about what should be done, and not how it should be done, worker may be an **independent contractor**

**2. Financial Control**

Whether the business has a right to direct or control the financial and business aspects of the worker’s job
Financial Control Factors-
Independent Contractor
- Worker bears profit or loss
- Worker has investment in business/materials
- Services available to the general public, licensed, insured, webpage, yellow pages
- Paid upon delivery of services or completion of specifics not based on time

3. Relationship
How the worker and the business organization perceive their relationship

Relationship factors-employee
- Any benefits are provided
- Ongoing office or other space is provided
- Worker has duties integral to the organization
- Attends office functions and training
- Has access to employer secure software
- Has U email or U directory listing
- Other employees do the same thing
Relationship factors-independent contractor
• Written contract
• Generally part time since they are serving other clients or full time for a fixed period
• Can be terminated according to contract
• Work offsite or if onsite, temporary
• Do not attend U functions or regular office meetings

Policy and Procedural Considerations
• Policy 3-111 governs U independent contractors and consultants

Policy 3-111 key provisions
– Employer-Employee Relationship:
  • A relationship that exists when the university has the right (whether or not it exercises the right) to supervise and control the manner of performance as well as the result of the service.
– Independent Contractor Relationship:
  • A relationship that exists when the university has the right to control only the result of the service, not the manner of performance.
Policy 3-111 key provisions

- Employee/Independent Contractor Classification Checklist must be duly executed before payment for consulting or professional services can be made to an independent consultant or independent contractor.

Policy 3-111 key provisions

- The use of consulting and professional service agreements under this Policy and Procedure is expected to be infrequent and primarily for the purpose of solving clearly delineated problems of short-term duration or to provide specific expertise not otherwise available.

Policy 3-111 key provisions

- The standard Consultant/Independent Contractors Agreement should be used
  - However, General Counsel or VP can OK another contract
Policy 3-111 key provisions

- An employee of the university may be engaged as a consultant or to provide professional services as an independent contractor only if the contract services to be performed ...

University employee

- (a) are not within the normal performance expectations of the university arising from the employee's university position,

- (b) are to be performed outside of the normal working time and work assignment of the employee and not under the direction, supervision, or control of the university,
• (c) do not involve a conflict of interest prohibited by the Utah Public Officers’ and Employees’ Ethics Act (see Policy 1-006), and

• (d) are to be provided across departmental lines, i.e., are not to be performed for an officer or principal investigator who holds an appointment in the same academic department or other operating unit as the contractor.

• However, 3-111.H. provides that if the independent contractor is an employee, payment must be requested as additional comp.
• Independent contractors on grant or contract have to have agreement signed off by Office of Sponsored Projects

Payments to Foreign Independent Contractors/Consultants
• Foreign Consultant and Independent Contractors who perform services within the U.S. require the same paperwork as a U.S. individual plus additional documents & may have required withholding

Payments to Foreign Independent Contractors/Consultants
• Need to route through Tax Services to ensure proper paperwork and withholdings
The University of Utah employee/independent contractor classification checklist

- Based on IRS 20 factors
- Must be completed
- Is not black and white since classification is not black and white
- Discuss

Questions? Contact…

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