

The Quagmire of Independent Contractor v. Employee Classification

- What is a business' risk of misclassifying workers?
- How do you tell an independent contractor from an employee?

A business owner would often prefer to have the worker be an independent contractor – fewer rules and laws apply to protect and give benefits to a worker who is an independent contractor. However, if the business classifies a worker improperly, the business has a lot of risk.

The Risk: There really is no risk if you classify a worker as an employee (other than the normal issues and expenses - like benefits - of having employees instead of independent contractors). The problem comes when you classify a worker as an independent contractor when they should be an employee. The risks include:

IRS problems for failing to pay FICA and similar taxes on their income, and failure to withhold income taxes from their paycheck

Workers' Compensation claims from the "employee" when you did not cover them under your workers' compensation insurance.

Unemployment claims from the "employee" (and possible state penalties) – when you did not cover them under your unemployment insurance

Problems with your retirement plans when the "employee" could later claim retirement benefits and the business would not have planned for that. The US Department of Labor could possibly be involved.

Classification Rules: The specifics to determine whether a person is an employee or an independent contractor depends on the purpose for making that determination, e.g., the classification for IRS purposes may be different than classification for workers' compensation coverage or unemployment compensation or other reasons. However, the general rules are similar.

Two indications that the worker is more likely an independent contractor are: (1) the worker does similar work for several businesses, and (2) the worker took steps to actually do that activity in an entity rather than as an individual. Another way to phrase this is that an independent contractor is free from control and direction from the

employing business, and that the worker is customarily engaged in an independent trade, occupation, profession or business related to the service performed.

Further written agreements between the worker and the employing business are certainly helpful to show independent contractor status. Colorado law has some specific requirements for those agreements.

For further information, please contact:

Barbara J. Wells
650 S. Cherry St., Suite 1100
Denver, CO 80246
bwells@minorbrown.com
303-320-1053
www.minorbrown.com

This information is for general purposes only and is not intended to constitute any specific legal advice of any type.