

What Employers Need to Know to Correctly Classify Employees and Independent Contractors

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No matter the time of year, businesses need to know the different employment classifications. In general, employers are required to withhold and remit certain taxes – federal and state income, Social Security, Medicare, and unemployment taxes – on behalf of employees but not for independent contractors. The gig economy has many individuals working multiple jobs, often preferring to be treated as self-employed independent contractors rather than have their paychecks reduced for these taxes, unemployment insurance, and other similar costs. However, in the event of a misclassification of a worker, a business can be held liable for these unpaid taxes in addition to being assessed significant noncompliance penalties.

The crux of worker classification is determining what level of control a business has over the worker. Specifically, does the business have the right to control how a worker performs his or her job? The IRS and the respective State's Department of Labor assesses a company's control of the parties' behavioral connections, financial affiliation, and overall type of relationship. The analysis can be summed up with some basic questions, including:

- Does the business have the right to control the details of what the worker

does, where they do it, and how they do it?

- Does the business control when and how the worker gets paid and whether expenses, supplies, and tools are subject to reimbursement?
- Is there a contractual relationship between the worker and business detailing the key aspects of the job, including project length, health or pension benefits, and vacation time?

Affirmative answers to these questions strongly indicate that an employer-employee relationship exists.

Conversely, when a worker identifies as a self-employed independent contractor, the following factors tend to be present:

- Operating a business under a limited liability company;
- Tracking hours worked and preparing invoices using such information;
- Rendering services for multiple businesses; and
- Determining one's own hours, deadlines, and use of personal tools or equipment.

Fortunately, for those businesses that may have misclassified a worker, there is an opportunity to obtain relief from some of the back tax obligations and penalty accruals. The IRS, like many states, has a voluntary compliance program allowing companies to reclassify workers as employees on a going forward basis, while settling their prior-year tax exposure. Participation in the program also offers responsible persons within the organization relief from being held personally liable for uncollected payroll taxes.

If you have questions about your company's employment classification and how you can ensure your tax responsibilities are being met, please contact [Alan Goldenberg](#), Principal and Leader of the State and Local Taxation and Tax Controversy groups, or your Anchin Relationship Partner.