

“Employee” vs “Independent Contractor” Classification

The issue of whether an individual is properly classified as an “independent contractor” depends upon the particular law under which the analysis is being made. Different governmental agencies apply different legal tests for independent contractor status. The Internal Revenue Code, Fair Labor Standards Act, Wisconsin Workers’ Compensation Act and Wisconsin Unemployment Insurance Act each apply tests to make their determinations.

In all cases, it is the employer’s burden to prove that an individual meets the requirements under the legal test(s) applied. Neither the label used by the parties, nor the use of a written agreement is determinative. Moreover, one agency’s determination is not binding on another agency. Therefore, an individual could be considered an independent contractor for tax purposes, but an employee for workers’ compensation purposes.

Significant Liability for Misclassification

Take a conservative approach when deciding whether to classify an individual as an independent contractor. The consequences for misclassification are significant. It can result in penalties, fines, forfeitures and other liability. For example, an employer could be ordered to pay workers’ compensation benefits to an injured worker that the employer did not consider its employee. Governmental agencies will almost by default initially conclude that an employer/employee relationship exists and force you to litigate the issue.

Minimize Your Liability

Reduce your liability exposure by following these guidelines:

- Closely analyze the relationship between the parties and apply all of the applicable legal tests for independent contractor status. If your company is not confident that it can satisfy all factors of each test, assume the individual is an employee and not an independent contractor.
- Have your attorney prepare independent contractor agreements for all such relationships.
- Make certain that your independent contractors own stand-alone business entities (LLC’s, etc.) with separate business offices, and that they hold themselves out to the public as the operators of a separate business (e.g., Yellow Page ads, etc).
- Avoid individuals who are largely dependent upon your company for their livelihood, who perform work also being performed by your employees, or who work as part of a crew assembled by your company.
- Don’t classify the same individual as an employee for some jobs and as an independent contractor for others.
- Get written invoices for all jobs.