ROBINSON PAYNE LLC

RPLLC Summary Sheet
The Independent Contractor vs Employee Dilemma

As Rich Payne noted in a recent RPLLC Blog, there are actually 3 different standards or tests being used to determine whether a worker is an employee or independent contractor. Illinois courts use a common law "right to control" test, the US Department of Labor (DOL), under the Fair Labor Standards Act, uses an "economic reality" test, and the IRS uses a 20-factor test. All these tests have one thing in common: how much control does the employer exercise over the activities of the worker?

So, what are these tests?

The courts' common law "right to control" test consists of the following 10 factors: (1) the extent of control which, by agreement, the hiring party may exercise over the hired party; (2) whether the hired party is engaged in a distinct occupation or business that is usually done by a specialist without supervision; (3) how the worker's staff are hired and whether they are paid by the hiring party or the worker; (4) the skill required in the particular occupation; (5) which party supplies the means, tools, and place of work; (6) the length of time for which the person is hired; (7) the method of payment, whether by time or the job; (8) whether the work is part of the regular business of the hiring party; (9) whether the parties believe they are creating an employment relationship; and (10) whether the hired party is an actual business entity.

The FLSA test of "economic realities" includes: (1) the degree of control exercised by the hiring party over the manner in which the work is performed; (2) the relative investments by the hiring party and the worker in materials and equipment; (3) the degree to which the worker's opportunity for profit and loss is determined by the hiring party or the worker's own financial acumen and management skill; (4) the skill and initiative required in performing the job; (5) the permanency of the relationship; and (6) whether the service is an integral part of the hiring party's business.

The IRS test considers 20 factors. Included in those are: (1) how much instruction is provided (employees typically must follow instructions as to when, where, and how to perform the job); (2) training (requiring training supports employee status); (3) integration of the worker's services into the business operations suggests that the hiring party directs and controls the worker; (4) whether services are rendered personally by a specific worker, suggesting the hiring party controls the methods used to complete the work; (5) whether there is an ongoing relationship, which suggests that an employer-employee relationship exists; (6) whether the establishment sets hours of work, implying control over the worker; (7) whether full-time work is required, which suggests control over the worker; (8) whether the hiring party provides tools and materials, which suggests an employer-employee relationship; (9) whether the worker serves more than one firm, which generally supports an independent contractor relationship; and (10) whether the hiring party may discharge the worker at any time, indicating an employer-employee relationship.

As you can see, assessing your situation can be a complicated matter, on which you probably will need input from both your legal counsel and accountant. Don't go this one alone.

Here is a little more advice, once you've complied with the tests. To keep from running afoul of the law and misclassifying your workers, you need to understand these tests and comply with each of them. If at all possible, enter into independent contractor agreements with only contractors which are separate legal entities, i.e. LLC's or corporations. Always use a detailed, specific contract with an independent contractor which spells out the relationship as contractor and specifically disclaims employment, benefits, workers compensation coverage and all the other incidents of employment. (Be aware that a contract alone will not convince the IRS or DOL that an employee is actually an independent contractor). When contractors are doing things that are also done by employees, beware—that is a major indicator of misclassification. We hope no one will have an employee doing two jobs within the company, one of which is as an employee and one as a contractor. That is almost always a losing proposition.

Please contact us to schedule a complimentary 30-minute consultation with Rich Payne to discuss your situation. If you have any question at all whether or not you are blurring or crossing the line between employee and contractor, and how to structure these relationships properly, you should contact us today.

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