

*Sy Accountancy Corporation*

Member, American Institute of CPAs

704 Mira Monte Place, Pasadena, California 91101

Tel (626) 744-0200 • Fax (626) 744-0300 • vsy@victorsycpa.com • www.victorsycpa.com

**20 TESTS FOR INDEPENDENT CONTRACTORS**

By Victor Sy, CPA, MBA

The Internal Revenue Service (IRS) and the Employment Development Department (EDD) have stepped up employment tax audits that lead to worker reclassification from independent contractors (1099) to employees (W2). At stake are payroll taxes (FICA, Medicare, SDI, FITW, SITW). Of course, business owners prefer to classify workers as independent contractors to save payroll taxes. Of course, the IRS prefers to classify them as employees. As a result of these conflicting interests, the IRS has developed audit programs to “catch” employers who “misclassify” workers. The program can be painful for small businesses that may not be able to withstand the economic strain of paying back taxes along with penalties and interests. These audits are even more painful because IRS and EDD do not conduct annual audits. Instead, they examine three years at a time. Three years of taxes, penalties, and interests could break a small business. This type of audits could be a pain for labor-intensive industries such as nursing registries, elderly care facilities, and home health/care companies that send nurses and caregivers to the homes of clients and patients.

Use the following checklist to test if your workers are employees or independent contractors. A “yes” points toward an employer-employee relationship while a “no” is an indication of independent contract. There are no fixed rules as to how many items with “yes” and “no” make up your success or failure in a payroll audit.

Yes No N/A

1. Workers must comply with instructions. ....
2. Worker is trained by person hiring. ....
3. Worker's services integrated in business. ....
4. Worker must personally render services. ....
5. Worker cannot hire or fire assistants. ....
6. Worker relationship is continuing. ....
7. Work hours are preset. ....
8. Worker must devote full time to business. ....
9. Work is done on employer's premises. ....
10. Worker cannot control order or sequence. ....
11. Worker submits oral or written reports. ....
12. Worker is paid at specific intervals. ....
13. Worker's business expenses are reimbursed. ....
14. Worker is provided with tools, materials. ....
15. Worker has no significant investment in facilities. ....
16. Worker has no opportunity for profit or loss. ....
17. Worker does not work with other firms. ....
18. Worker does not offer services to public. ....
19. Worker may be discharged by liability. ....
20. Worker can terminate without liability. ....