



THE LAW ADVISOR

EMPLOYEE OR INDEPENDENT CONTRACTOR: HOW I SHOULD KNOW... AND WHY IT MATTERS

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Uber is one of the fastest growing “technology” companies in the United States. If you are not familiar, Uber describes itself as follows on its website: “Uber is evolving the way the world moves. By seamlessly connecting riders to drivers through our apps, we make cities more accessible, opening up more possibilities for riders and more business for drivers. From our founding in 2009 to our launches in hundreds of cities today, Uber’s rapidly expanding global presence continues to bring people and their cities closer.”

One of the key elements of Uber’s business model is the use of drivers whom Uber treats as independent contractors rather than as employees. Uber’s driver sign-up page reads as follows: “Uber needs partners like you. Drive with Uber and earn great money as an independent contractor. Get paid weekly just for helping our community of riders get around town. Be your own boss and get paid in fares for driving on your own schedule.” (Emphasis added.)

By treating its drivers as independent contractors rather than employees, Uber benefits in a multitude of ways: (1) not having to comply with minimum wage and overtime laws; (2) not having to pay social security and medicare taxes; (3) not having to provide workmen’s compensation, unemployment insurance, and other legally mandated benefits; (4) not being responsible for withholding income taxes; (5) not having to provide health insurance, pension, paid-time-off, and other benefits that are ordinarily required to hire the best personnel; and (6) not having to potentially deal with an organized (unionized) labor force. In return, drivers benefit primarily by being able to set their own hours and working as much or as little as they want, with Uber doing all of the “heavy lifting” when it comes to marketing the service provided by drivers to consumers.

Uber’s business model and its very survival could be in grave danger if Uber is wrong and its drivers are

really employees. The issue of whether Uber drivers are truly independent contractors has been addressed in a number of unemployment and other types of administrative and judicial proceedings around the country, with many more such actions pending. The results have been mixed. For example, last June a California labor commission ruled that an Uber driver was an employee. The Florida agency overseeing unemployment benefits recently ruled

by an employer (what will be done and how it will be done). This applies even if you are given freedom of action. What matters is that the employer has the legal right to control the details of how the services are performed.”

Unfortunately, there is no bright line set of rules that determine whether a person is an employee. Instead, the IRS will rely on a weighing of all relevant factors to make the determination. These factors generally fall into

IT IS VITAL THAT YOU PROPERLY CATEGORIZE THE PERSONNEL PROVIDING SERVICES FOR YOUR BUSINESS, AS THE COSTS FOR BEING WRONG CAN BE SEVERE. AN EMPLOYER WHICH MISCLASSIFIES EMPLOYEES AS INDEPENDENT CONTRACTORS WILL BE LIABLE FOR UNPAID EMPLOYMENT TAXES, UNEMPLOYMENT INSURANCE TAXES, AND WORKMEN’S COMPENSATION PREMIUMS.

the other way, finding that Uber drivers are independent contractors.

I have used the Uber example to illustrate the complexity of the employee/independent contractor dilemma. If Uber ultimately turns out to be wrong, and its drivers are more universally treated as employees, its business model may not be tenable. In the balance of this article, I will present a broad overview of the issue and discuss how the IRS determines whether personnel is properly classified and the ramifications for misclassifying an “employee” as an “independent contractor.”

IRS GUIDELINES

According to the IRS website, the general rule is that “an individual is an independent contractor if the payer has the right to control or direct only the result of the work and not what will be done and how it will be done. The IRS website goes on to state that you “are not an independent contractor if you perform services that can be controlled

3 categories: (1) behavioral; (2) financial; and (3) type of relationship. The behavioral factors focus on the employer’s level of control. The financial factor focuses on how the person is paid, whether the person is reimbursed for expenses, and whether the person or the employer supplies the person with the tools of his or her trade. The relationship factor looks at whether there is a written agreement with the employer, whether the person is entitled to benefits (like an employee), and whether the relationship is ongoing and will be a key part of the business.

The IRS website further provides the following, which is supposed to help employers:

“Businesses must weigh all these factors when determining whether a worker is an employee or independent contractor. Some factors may indicate that the worker is an employee, while other factors indicate that the worker is an independent contractor. There is no “magic” or set number of factors that “makes” the worker an employee

or an independent contractor, and no one factor stands alone in making this determination. Also, factors which are relevant in one situation may not be relevant in another."

If your head is spinning, do not fret as you are not alone.

WHAT IF I AM WRONG?

It is vital that you properly categorize the personnel providing services for your business, as the costs for being wrong can be severe. An employer which misclassifies employees as independent contractors will be liable for unpaid employment taxes, unemployment insurance taxes, and workmen's compensation premiums. In addition, misclassified employees may have claims against the employer for violations of minimum wage and overtime requirements under the Fair Labor Standards Act. The financial consequences of a misclassification can be crippling and could possibly even bankrupt a company.

RECOMMENDATIONS

If you are unsure as to whether a specific person or a specific group of personnel should be treated as an employee or independent contractor, I have two recommendations: (1) consult with your company attorney and have a full and detailed conversation regarding the person so that counsel can help you make an informed and (hopefully) correct determination; and (2) if in doubt, treat the person as an employee. Although I do not have statistical proof to support my theory, I would speculate that in situations that are "close calls," the IRS will err on the side that benefits the agency and its tax collection efforts, which means that the IRS will likely determine the person to be an employee. Although Uber, the pharmaceutical companies, and other major corporations may have the time, resources, and inclination to fight the IRS, I assume that most of the readers of *Cleaner Times* do not, and therefore I

recommend that you be very careful before classifying a person as an independent contractor in order to save a few bucks. The risk could very well outweigh the reward.

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